

# Auscap Long Short Australian Equities Fund

The Value of Absolute Return Investing  
Advisers Big Day Out 2018



# Disclaimer

This presentation is not a Product Disclosure Statement under the Corporations Act 2001 (Cth).

Information in this presentation is general information only and does not take into account a particular client's individual objectives, financial situation, needs or circumstances, nor does this presentation purport to contain all the information that a prospective investor may require in evaluating a possible investment in the Auscap Long Short Australian Equities Fund (Fund). A prospective investor should conduct their own independent investigation and assessment of the Fund before making any investment, including obtaining investment, legal, tax and accounting advice appropriate to their circumstances.

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# Contents

1. Auscap – Who are we?
2. What are Absolute and Relative Return strategies?
3. How is an Absolute Return strategy different?
4. The Benefits and Risks of Absolute Return Strategies
5. Case studies



# Auscap Asset Management Limited

- Auscap Asset Management is the Responsible Entity and Investment Manager for the Auscap Long Short Australian Equities Fund
- Established in 2012, assets under management ~\$634m
- Investment team has over 30 years of combined experience in Australian equities investing
- Value investors with a quality bias
- Focus on both capital preservation and appreciation
- Principals co-invested in the Fund



# Auscap Long Short Australian Equities Fund

- Invest only in Australian equities and cash
- Concentrated high conviction portfolio, 30-45 positions
- Variable beta, typically long biased, index unaware
- Long term investors with an investment horizon of 5 years
- Zenith and Lonsec recommended
- Available on multiple platforms



# Investment Characteristics

*Target: 10-15% lower than market risk opportunities at the stock level\**

## LONG

### High Quality

- Cash producing businesses with solid return on invested capital
- Transparent business models, selling products/services with which we are familiar
- Strong balance sheets
- High quality management

### Value

- Stock is priced below estimated intrinsic value

## SHORT

### Poor Quality

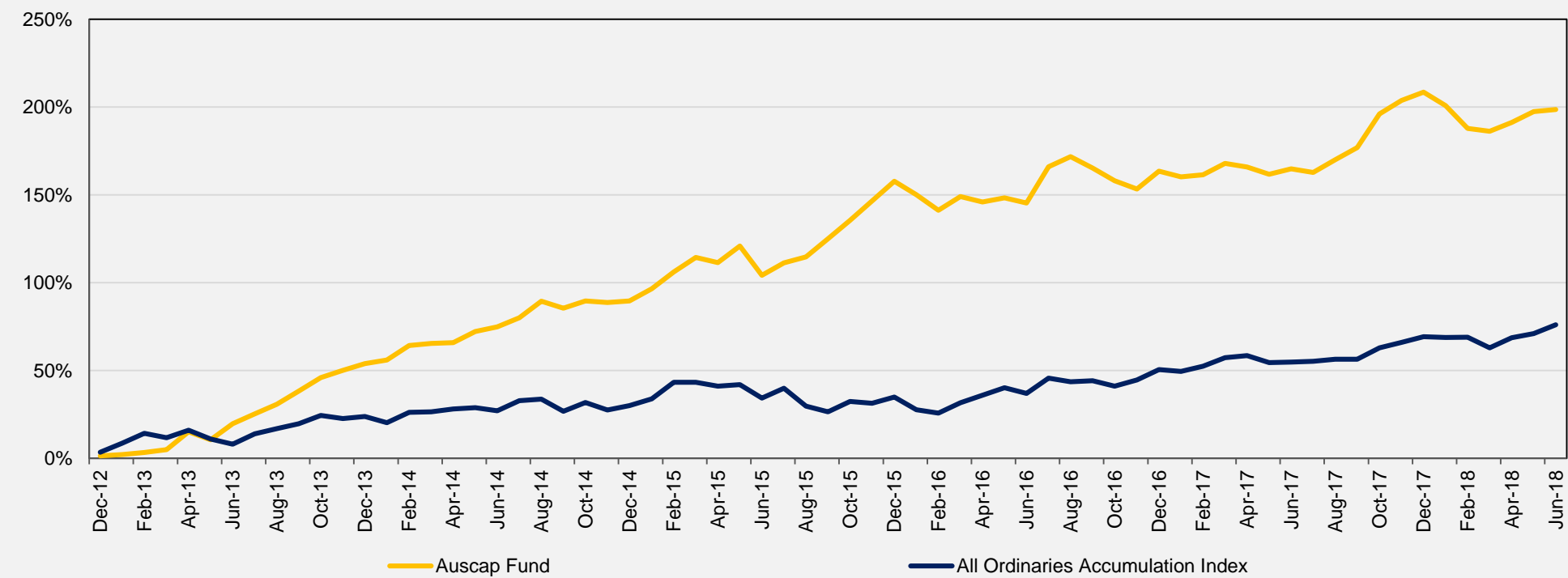
- Low quality earnings, poor or negative cash generation
- Complex business models
- Low ROIC, stressed balance sheets
- Inexperienced or promotional management
- Clear downside catalyst, such as earnings in a downgrade cycle

### Value

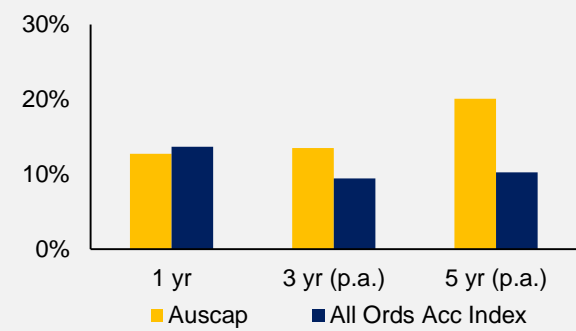
- Stock is trading significantly above estimated intrinsic value



# Performance\*



	3 mth	6 mth	1 yr	3 yr (p.a.)	5 yr (p.a.)	S.I (p.a.)
Auscap	4.3%	(3.2%)	12.7%	13.5%	20.1%	21.6%
All Ords A.I.	8.0%	4.0%	13.7%	9.4%	10.3%	10.7%
Outperformance	-3.7%	(7.2%)	(0.9%)	4.1%	9.8%	11.0%



\* Performance figures are calculated for the lead series net of all fees and expenses and assuming the reinvestment of all distributions. Actual performance may differ for investments made in different classes or series. Past performance is not a reliable indicator of future performance.  
Source: IRESS, Auscap



# What are Absolute and Relative Return strategies

## **Relative return funds**

Most funds are relative return focused - they aim to generate higher returns than the market.

## **Absolute return funds**

Absolute return funds are generally market agnostic - they aim to generate positive returns irrespective of market conditions.





# How is an Absolute Return strategy different?

## Differences

- Focused on absolute returns and absolute risks
- Do not have to be fully invested, can hold cash
- Index unaware
- Can invest long or short
- Positions are sized by conviction
- Can invest in alternative instruments



# The Benefits of Absolute Return Investing

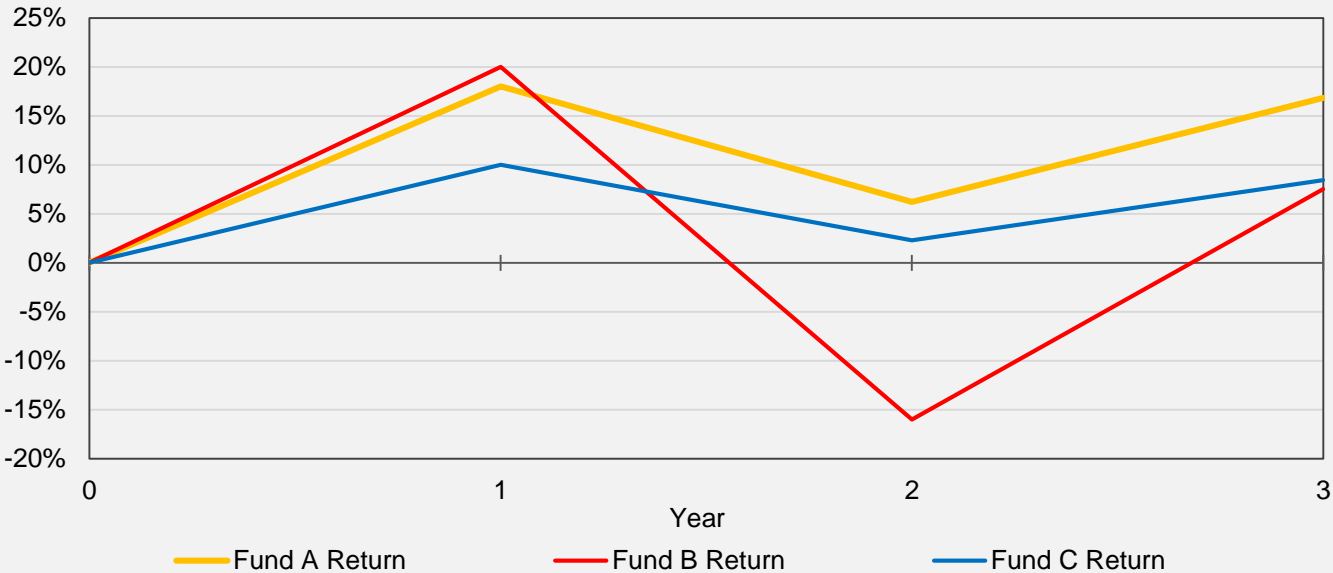
Absolute return strategies focus on absolute returns and absolute risks.

Year	Fund A	Fund B	Fund C
Year 1 Return	+18%	+20%	+10%
Year 2 Return	-10%	-30%	-7%
Year 3 Return	+10%	+28%	+6%
Simple Average Return	+6%	+6%	+3%
Average Compound Annual Return	+5.3%	+2.4%	+2.7%

**Benefit:**  
Can deliver better risk adjusted returns

**Risk:**  
Can underperform in a rising market

Compound Returns for Funds A, B & C



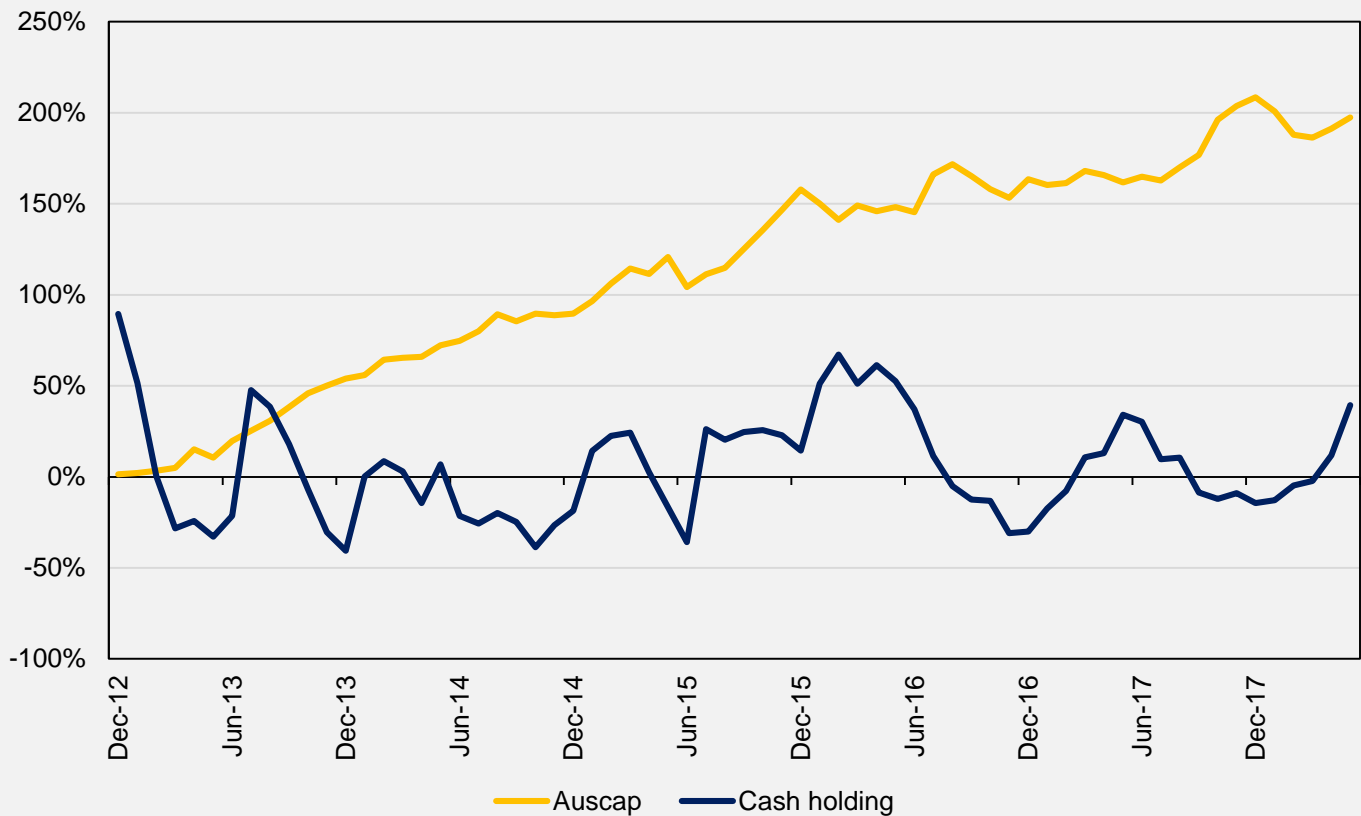
# The Benefits of Absolute Return Investing

Absolute return funds do not need to be fully invested. They can hold cash

**Benefit:**  
Preserves capital and gives optionality

**Risk:**  
Can underperform in a rising market

Auscap performance\* and cash holding



\* Performance is based on the lead series net of all fees and expenses and assuming the reinvestment of all distributions. Actual performance may differ for investments made in different classes or series. Past performance is not a reliable indicator of future performance.  
Source: Auscap

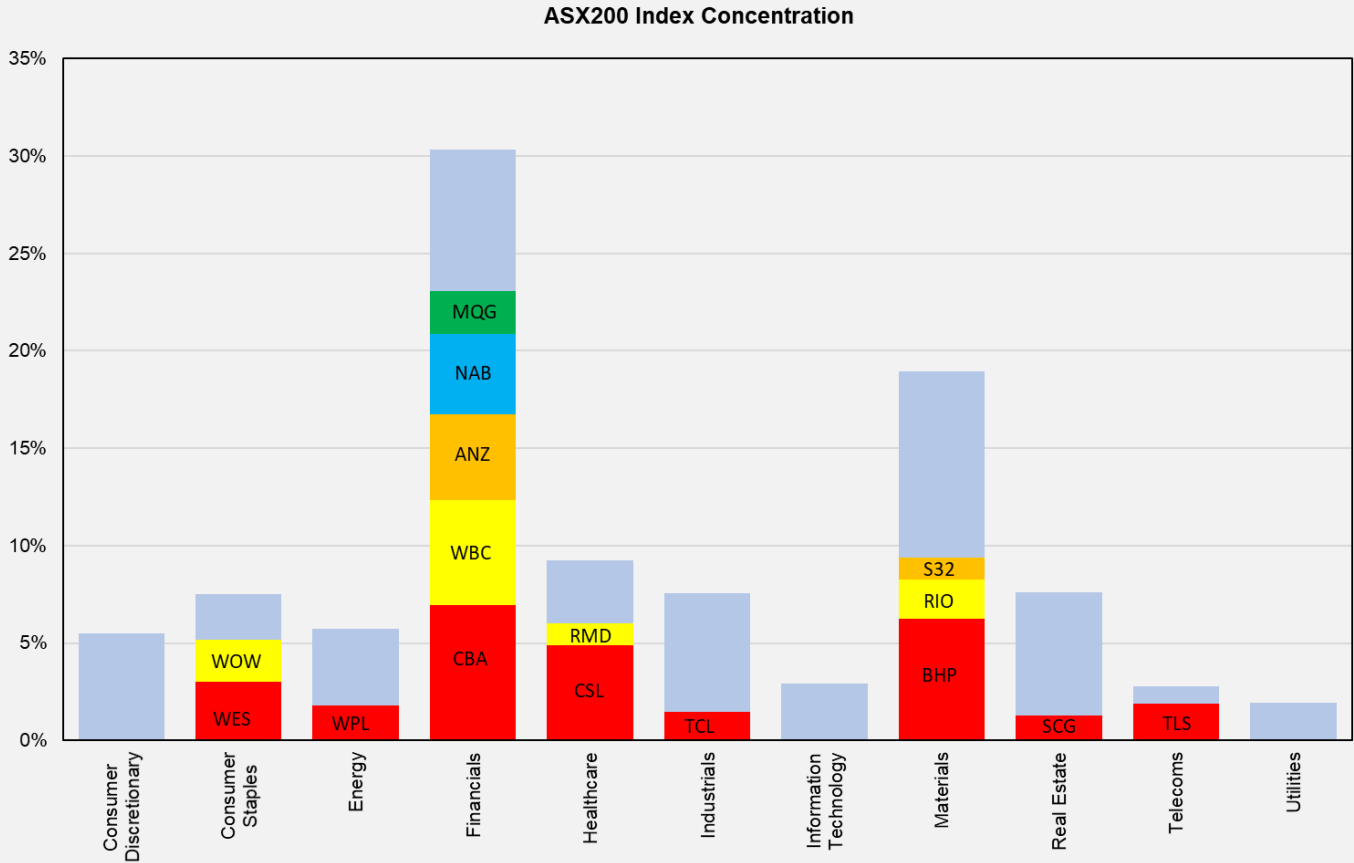


# The Benefits of Absolute Return Investing

Absolute return strategies are index unaware

**Benefit:**  
No passive positions

**Risk:**  
Can underperform in a market where sectors that aren't held do well for the broader market



16 companies make up 50% of ASX200



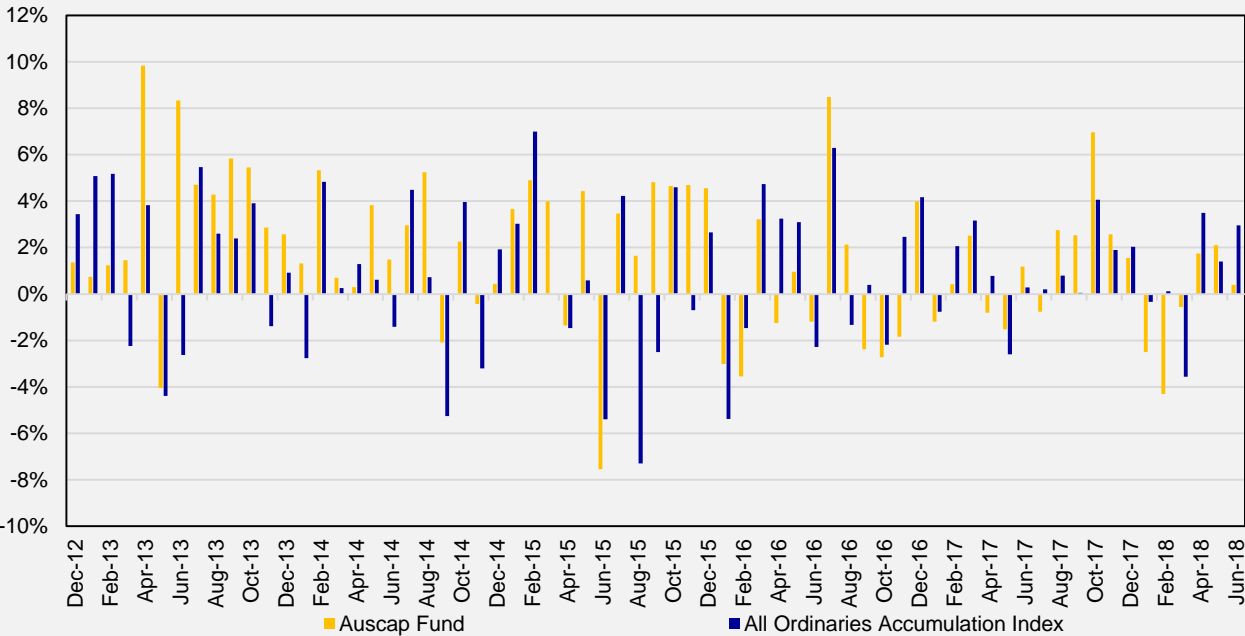
# The Benefits of Absolute Return Investing

Absolute return strategies can invest long or short

**Benefit:**  
Broadens opportunities to generate returns/protect capital

**Risk:**  
Asymmetry of risk on short positions

Auscap Long Short Australian Equities Fund vs All Ordinaries Accumulation Index



	Auscap	All Ords
Average annual returns	21.6%	10.7%
Annualised standard deviation	11.3%	11.0%
Average positive months	2.6%	2.7%
Average negative months	0.0%	-2.6%
Number of positive months	48	44
Number of negative months	19	23

\* Performance is based on the lead series net of all fees and expenses and assuming the reinvestment of all distributions. Actual performance may differ for investments made in different classes or series. Past performance is not a reliable indicator of future performance.  
Source: IRESS, Auscap



# The Benefits of Absolute Return Investing

Absolute return strategies can invest in alternative instruments

**Benefit:**

Additional ways to add to returns

**Risk:**

Increased risk from liquidity, leverage and participation  
in alternative asset classes

**Auscap invests only in Australian shares and cash**

## Alternative Instruments

- Equity/Index futures and options
- Commodities
- Unlisted securities
- Foreign exchange
- Interest rate derivatives
- Pre-IPO companies
- Exotic/OTC derivatives
- Fixed Income securities
- Hybrids/Convertibles



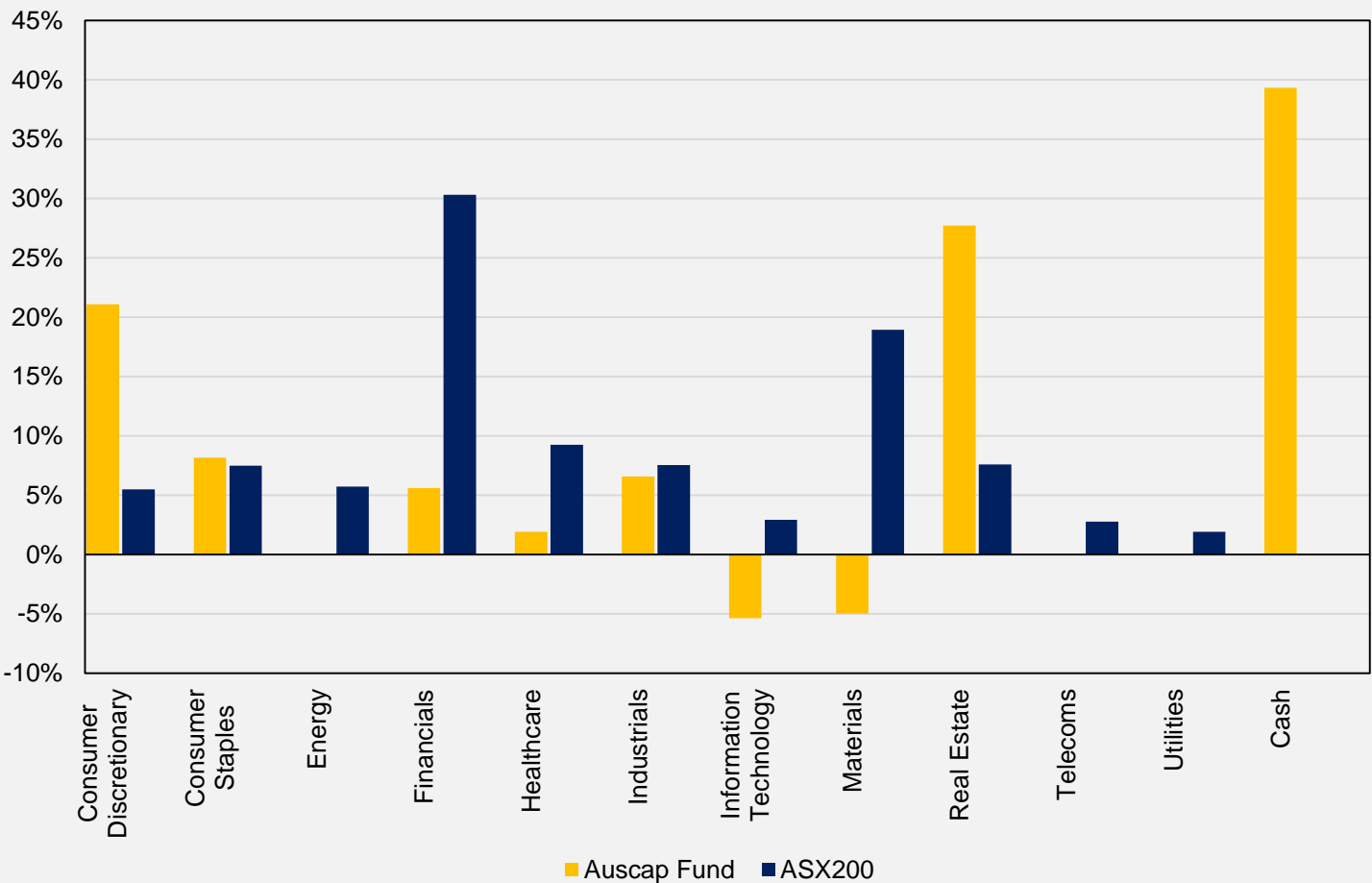
# The Benefits of Absolute Return Investing

Absolute return strategies can size position by conviction

**Benefit:**  
Highest portfolio weightings in best ideas

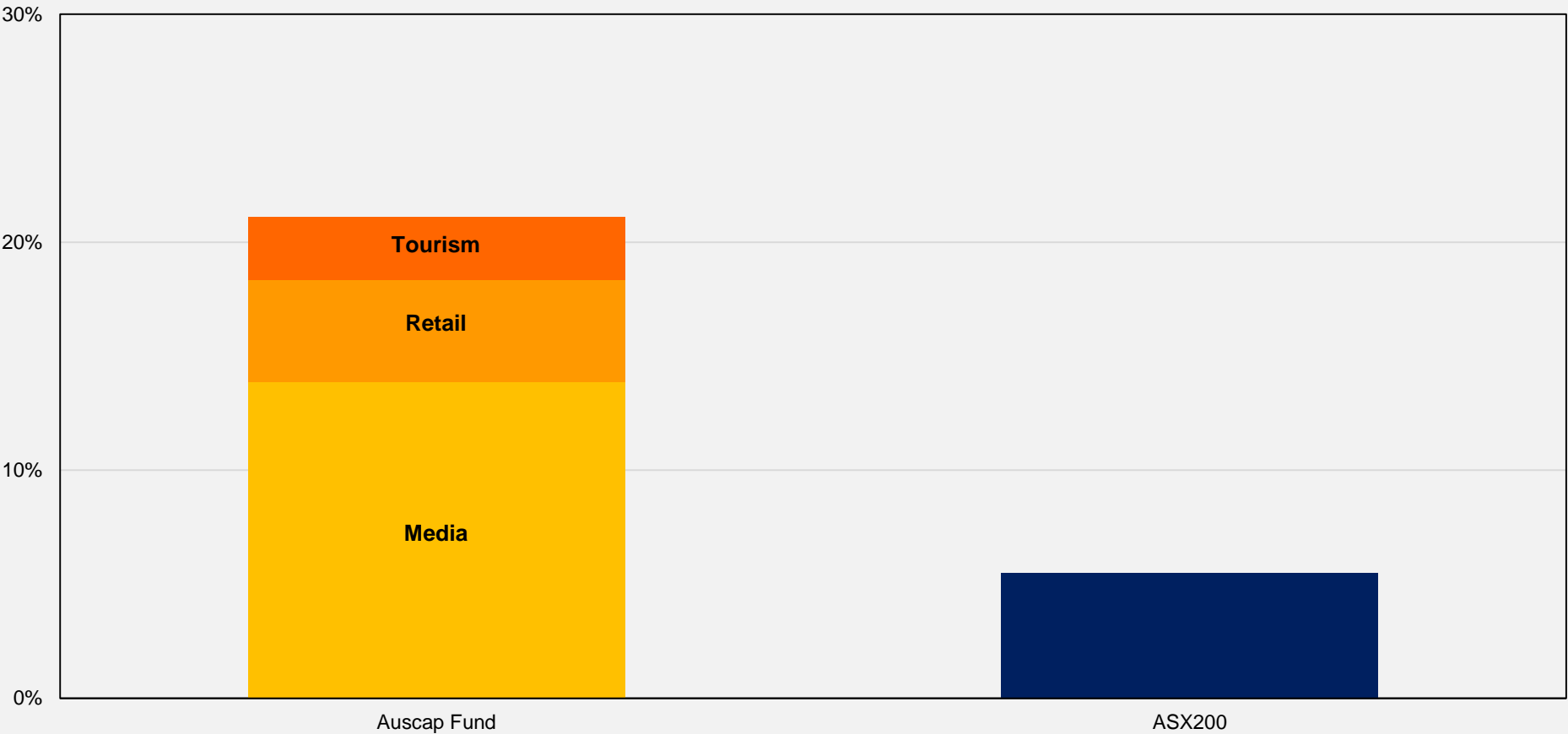
**Risk:**  
Some concentration risk

Auscap Fund Portfolio (Net exposure)



# Auscap: Consumer Discretionary

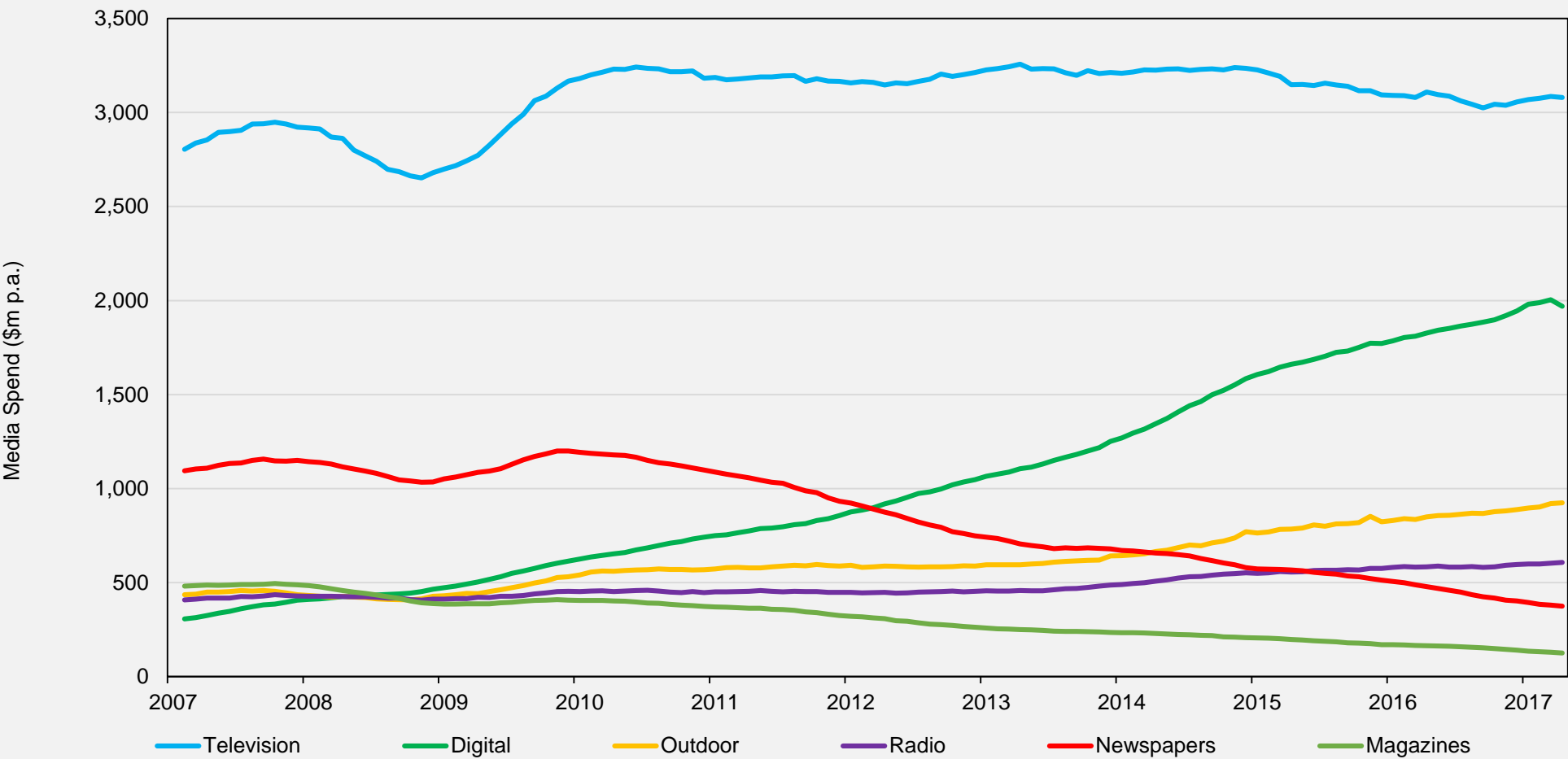
Current Portfolio - Consumer Discretionary





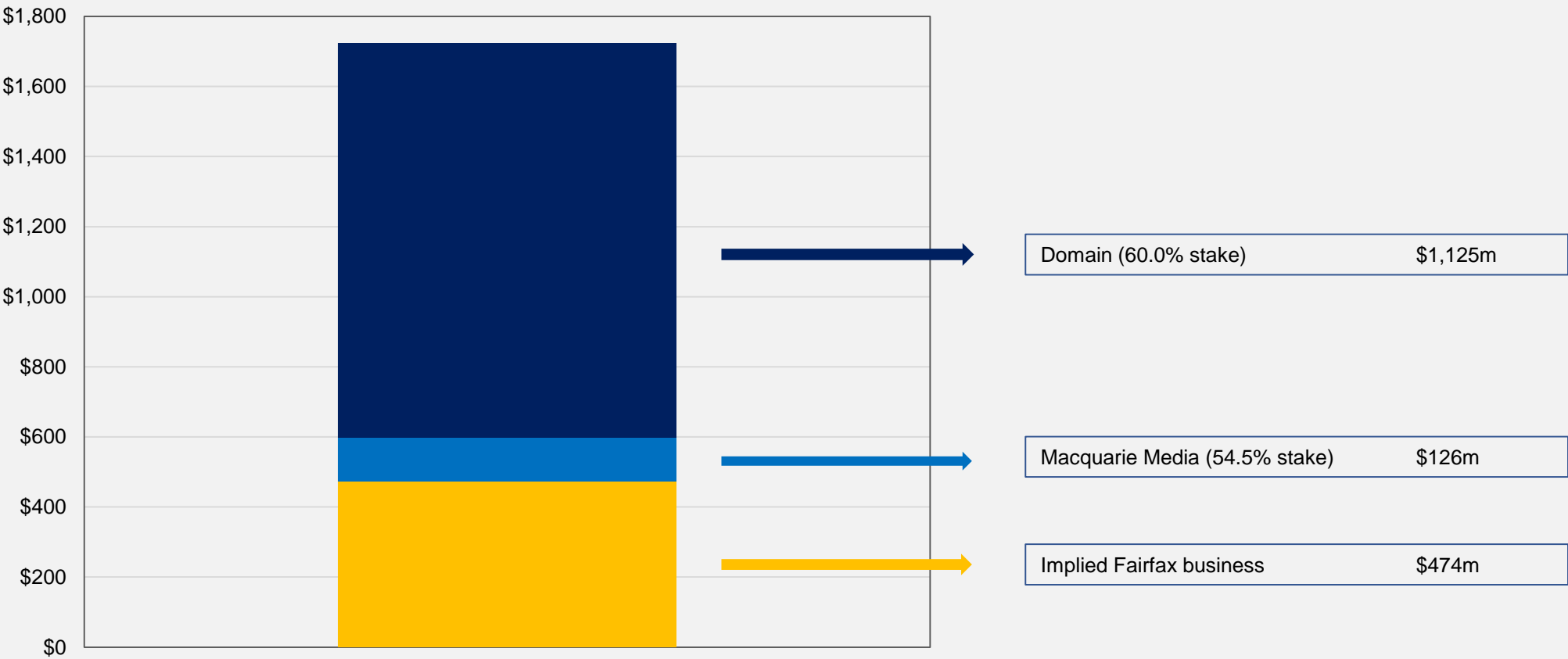
# Auscap: Media

Australian Media Spend



# Auscap: Media

Fairfax Sum-of-the-Parts Valuation (\$m)\*



# Auscap: Media

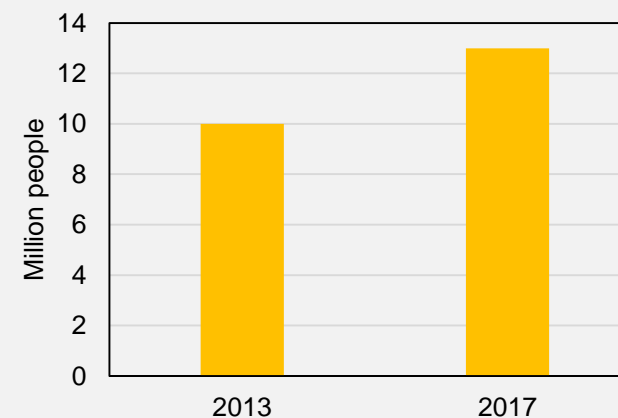
## 2018 H1 Performance

Business unit	EBITDA (1H FY18)
Metropolitan Media (SMH, Age, AFR)	\$30.0m
Australian Community Media	\$36.4m
Stuff (NZ Business)	\$18.9m
Less corporate costs	-\$13.2m
<b>2018 H1 EBITDA</b>	<b>\$72.1m</b>

Implied valuation  
3x EBITDA

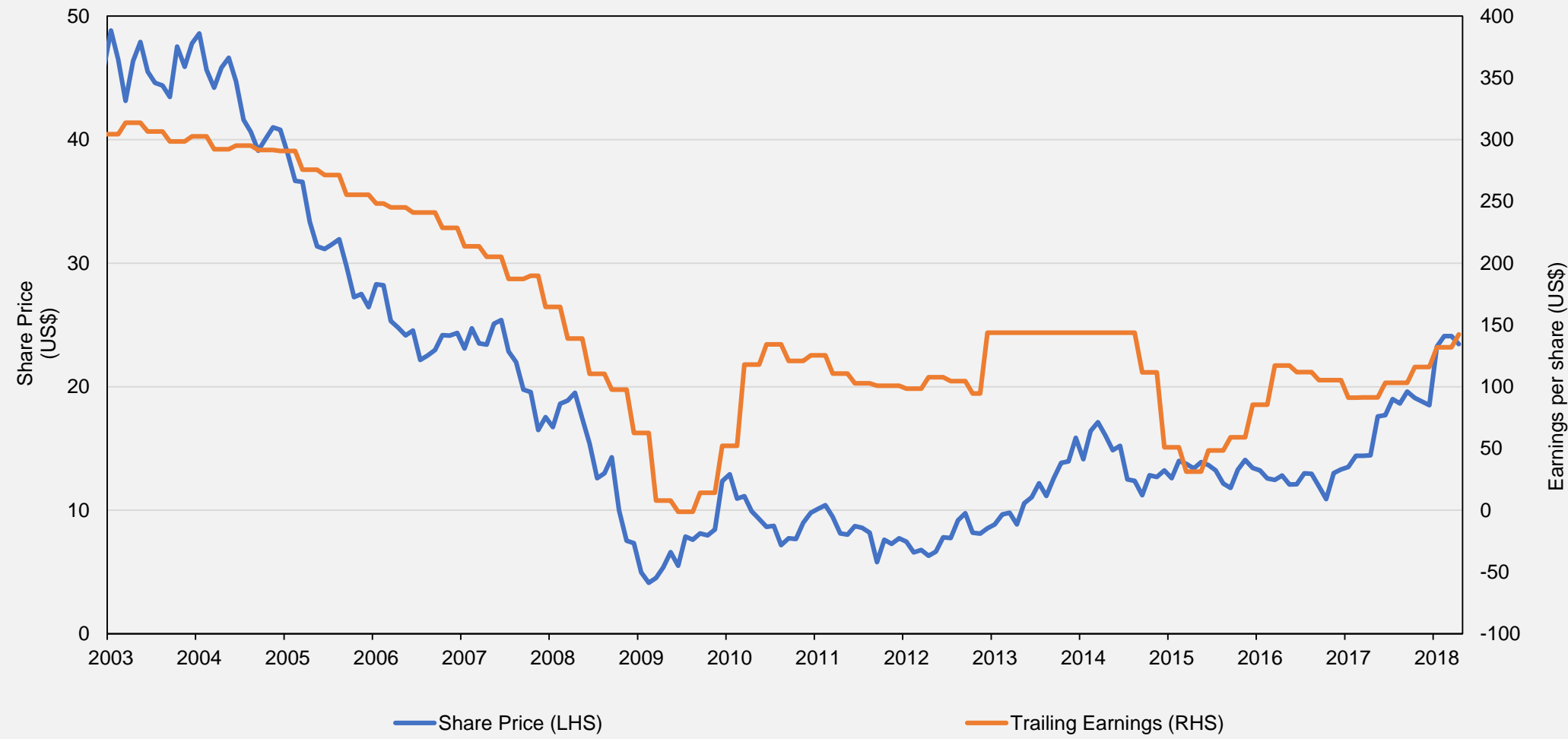
Additional growth options
Stan
Drive, RSVP, Weather Zone
New digital ventures

Fairfax publishing audience



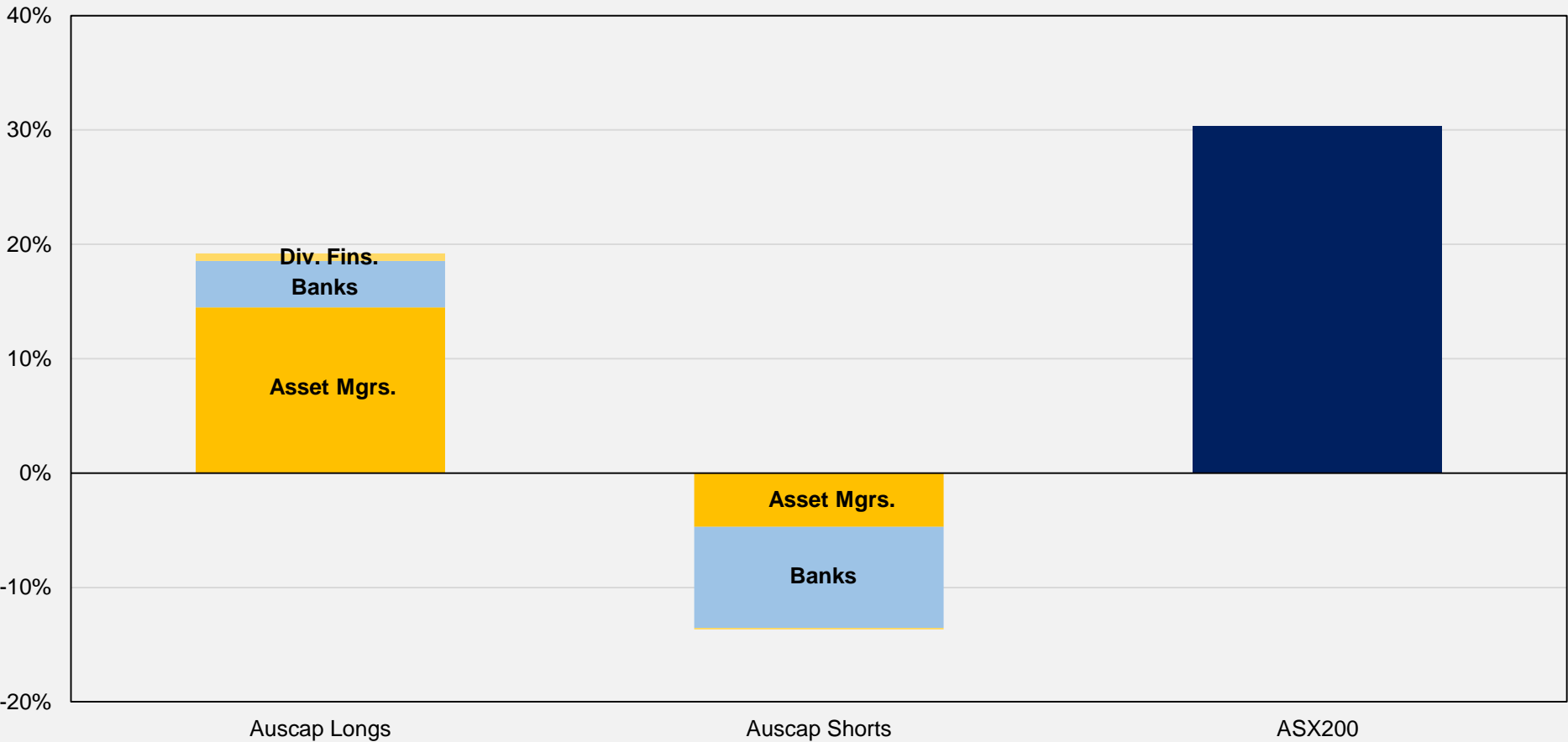
# Auscap: Media

New York Times - Share Price and Earnings



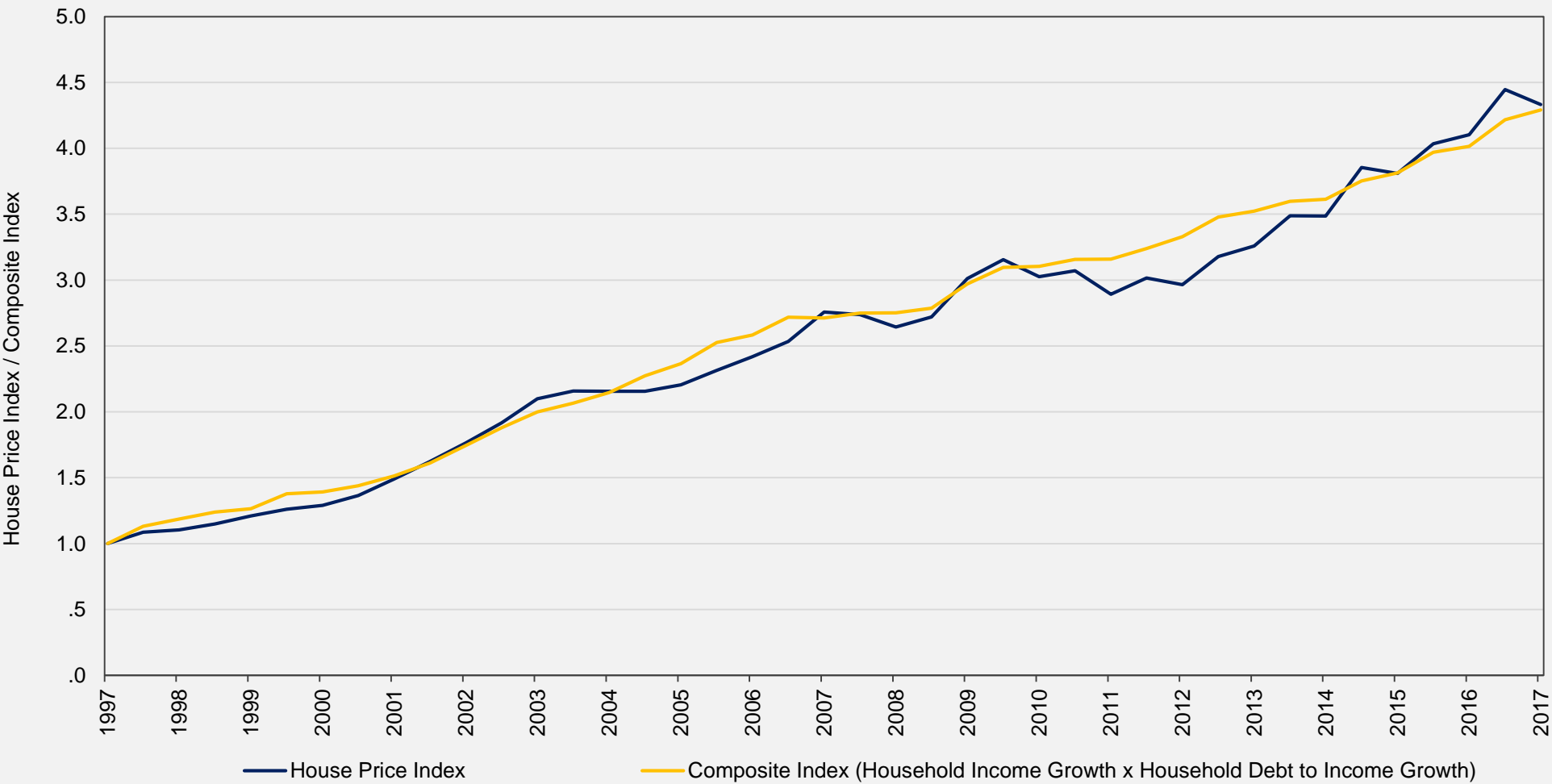
# Auscap: Financials

Current Portfolio - Financials



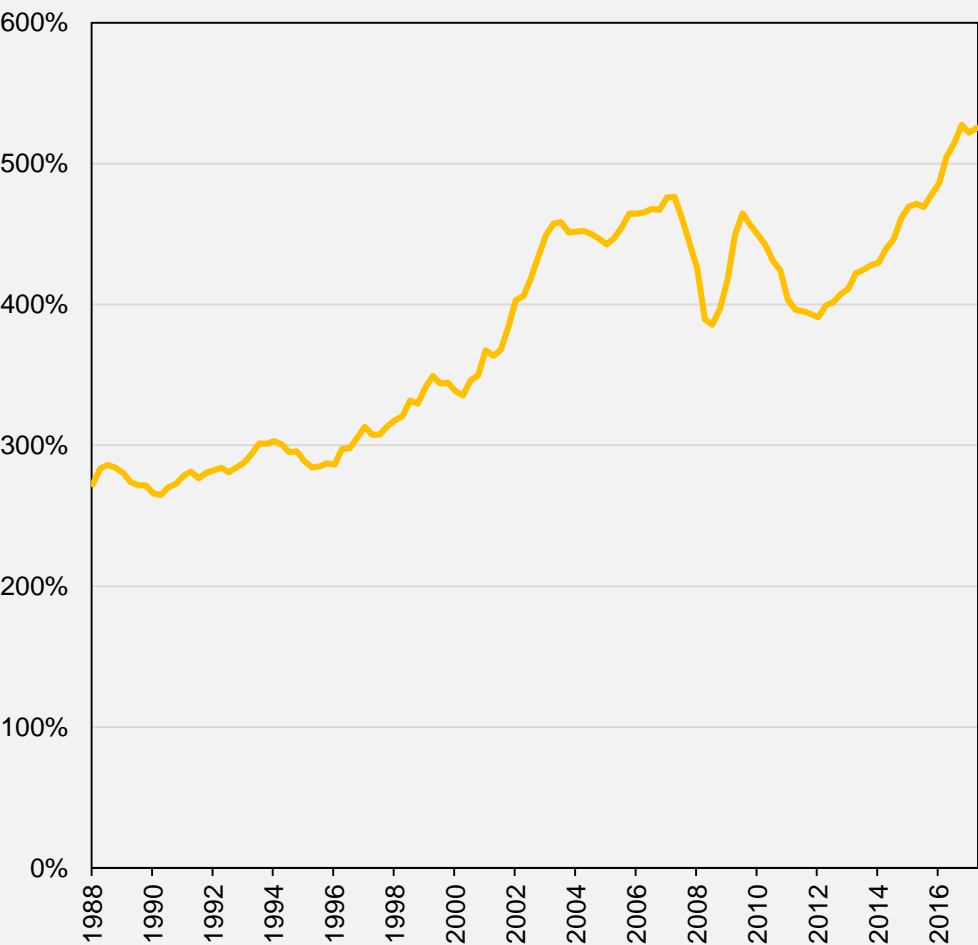
# Auscap: Financials

House Price Growth vs Composite Index

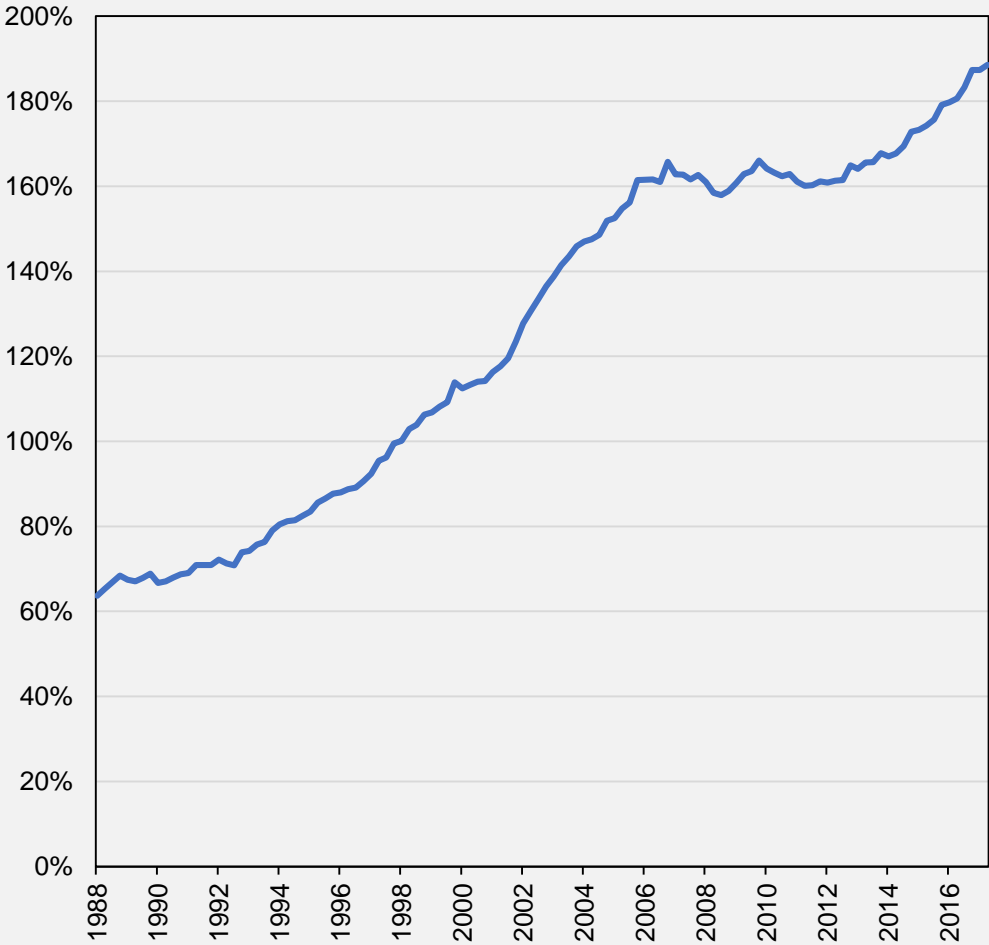


# Auscap: Financials

Housing Assets as a Ratio to Disposable Income

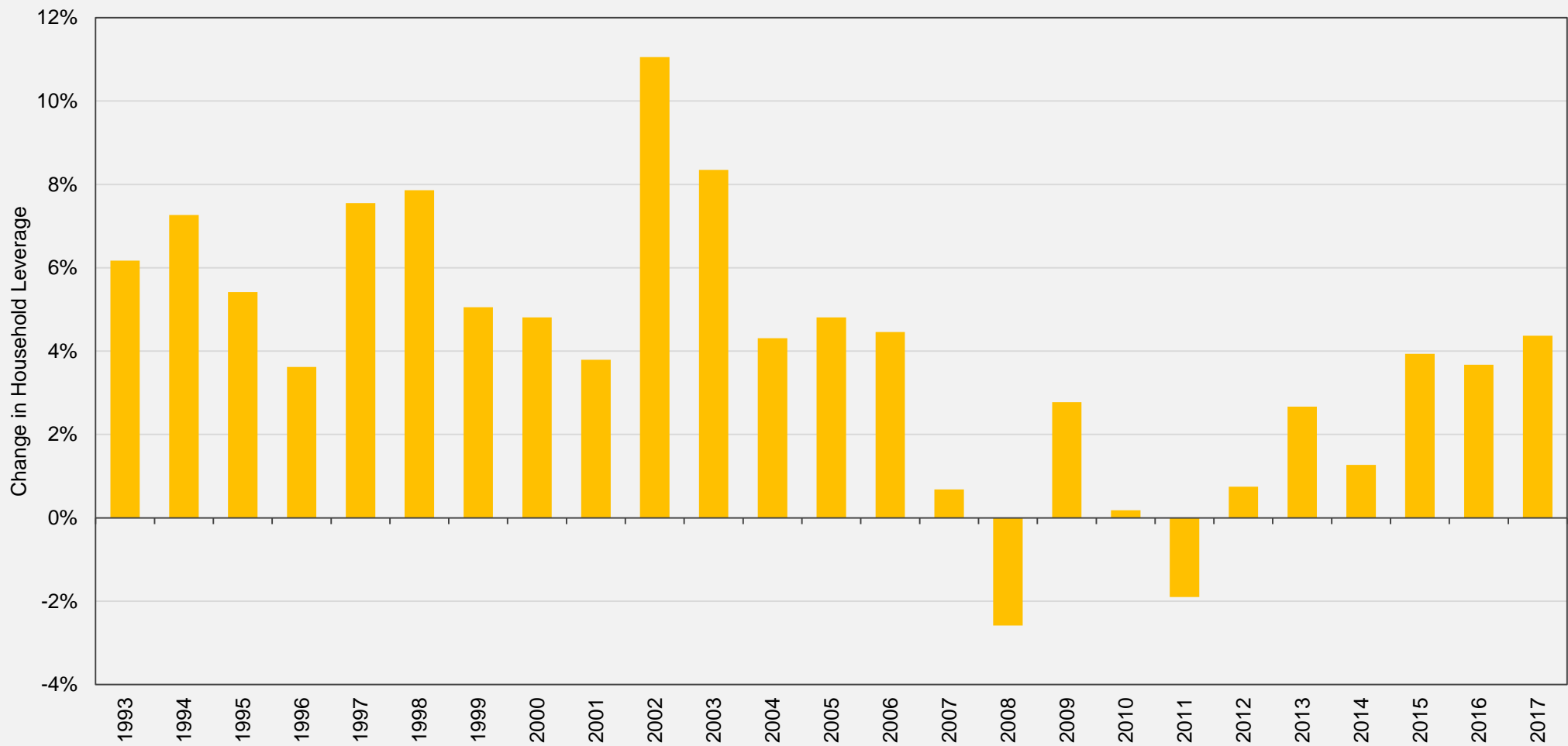


Household Debt as a Ratio to Disposable Income



# Auscap: Financials

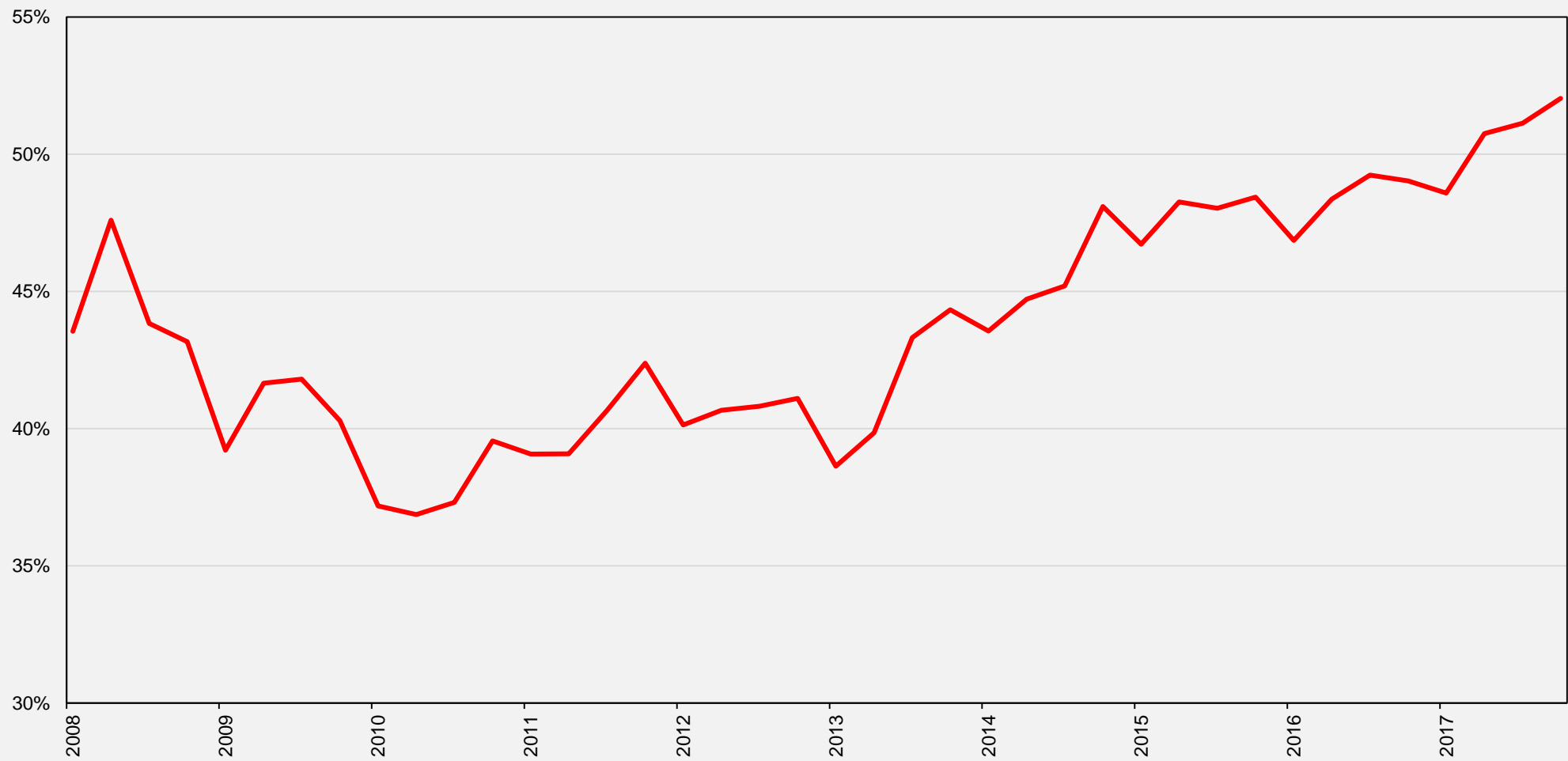
Change in Household Leverage (Household Debt to Income Ratio)





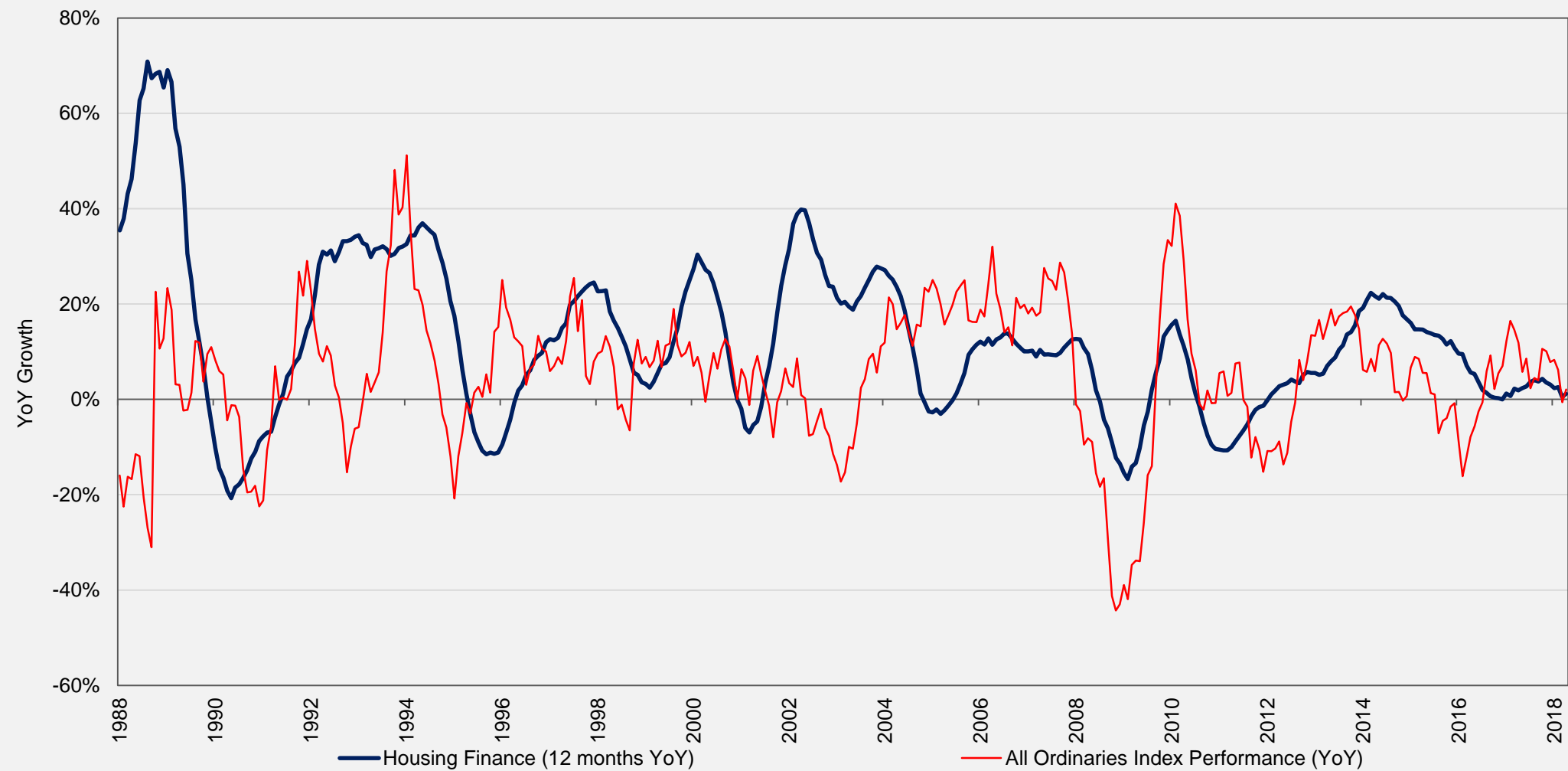
# Auscap: Financials

% Bank Residential Loans Approved - Originated from 3rd Parties/Brokers

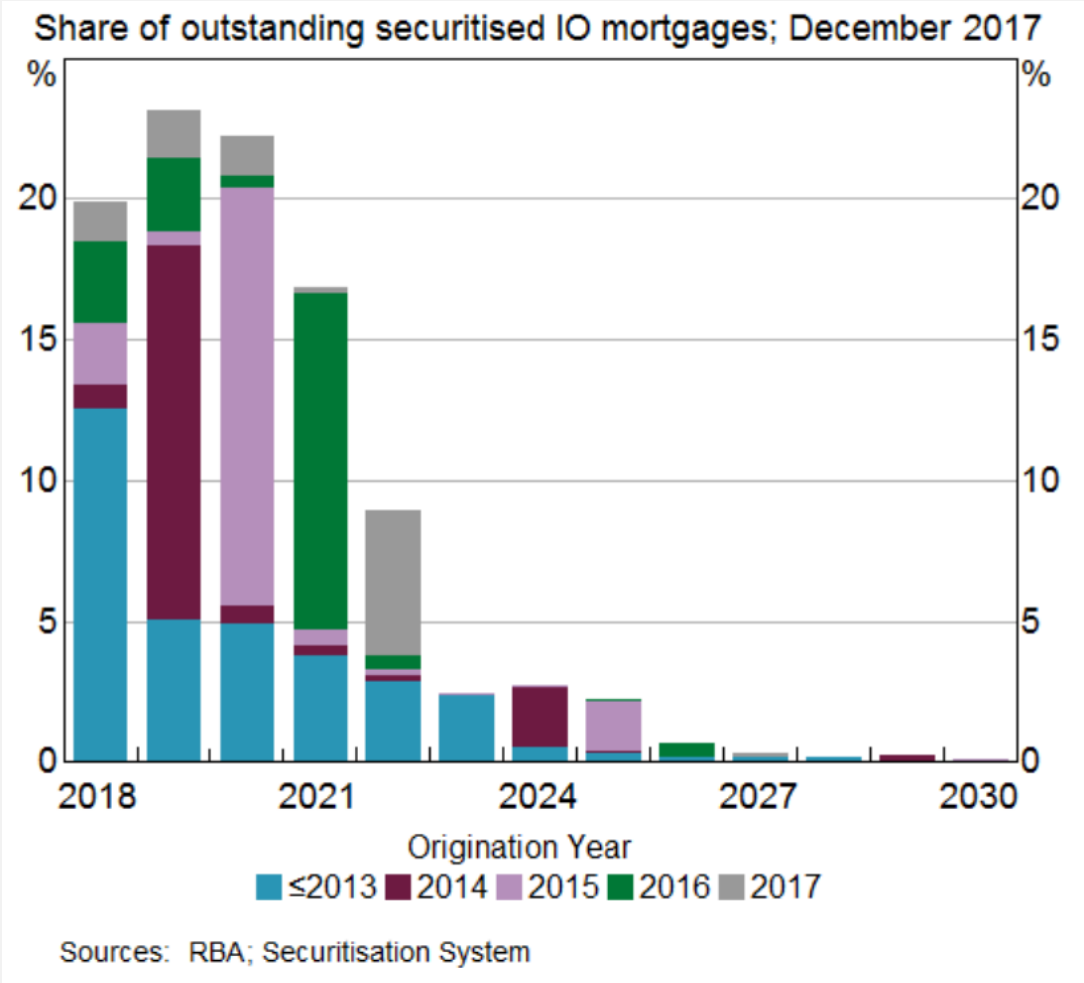


# Auscap: Financials

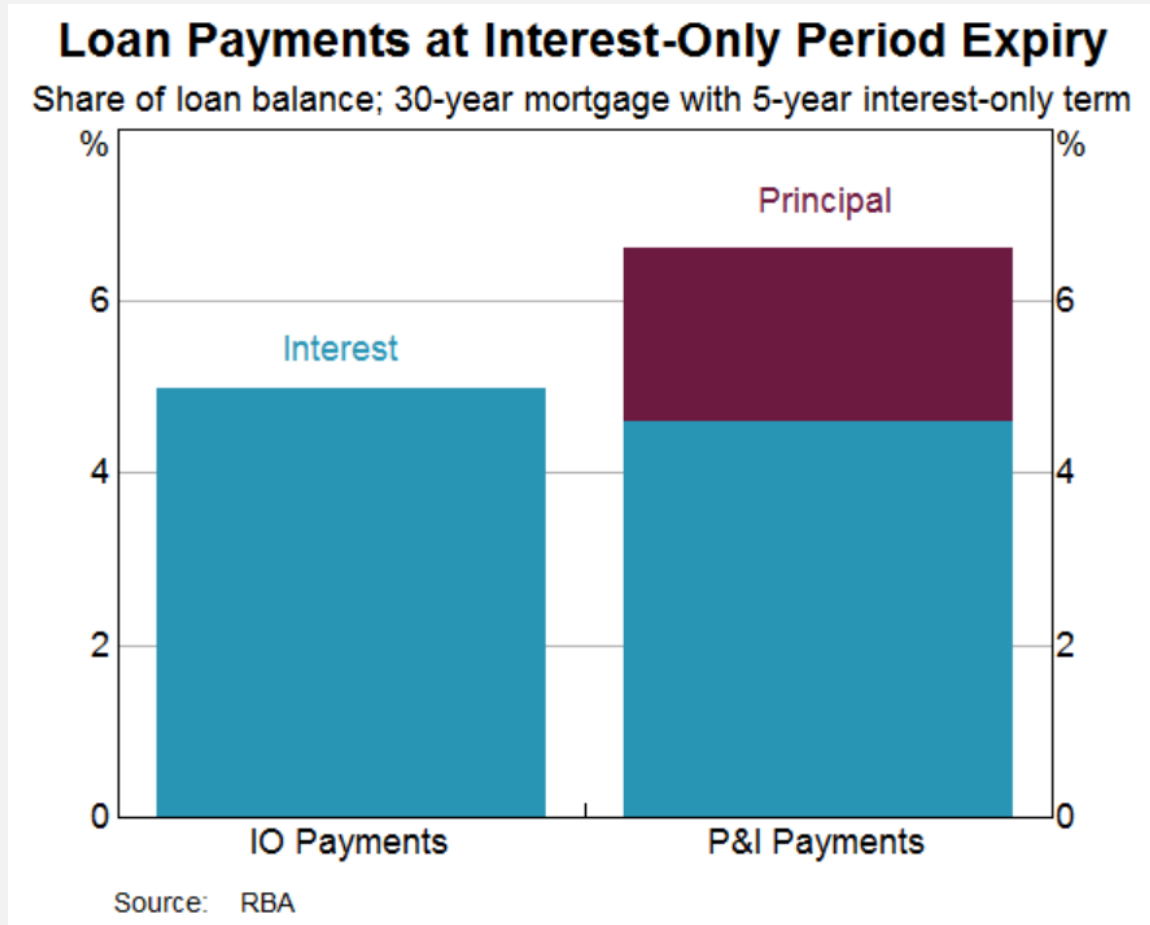
Housing Finance Growth vs All Ordinaries Index Performance



# Auscap: Financials



# Auscap: Financials

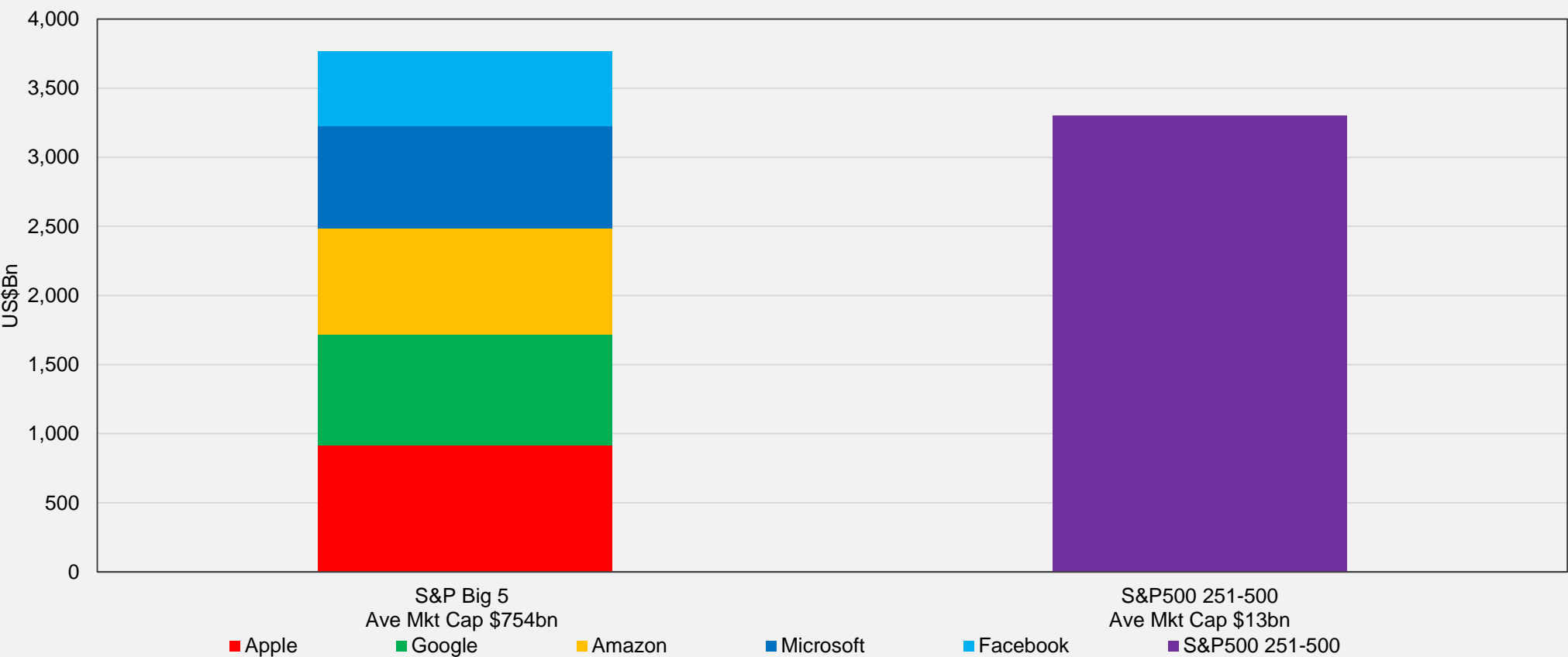


# Auscap: Financials

## Dominance of the Big 5 US technology companies

- 15% of the S&P500; Equivalent to the bottom 271 stocks in the S&P500 by market capitalisation

S&P500 Concentration: the Big 5 US Technology Companies

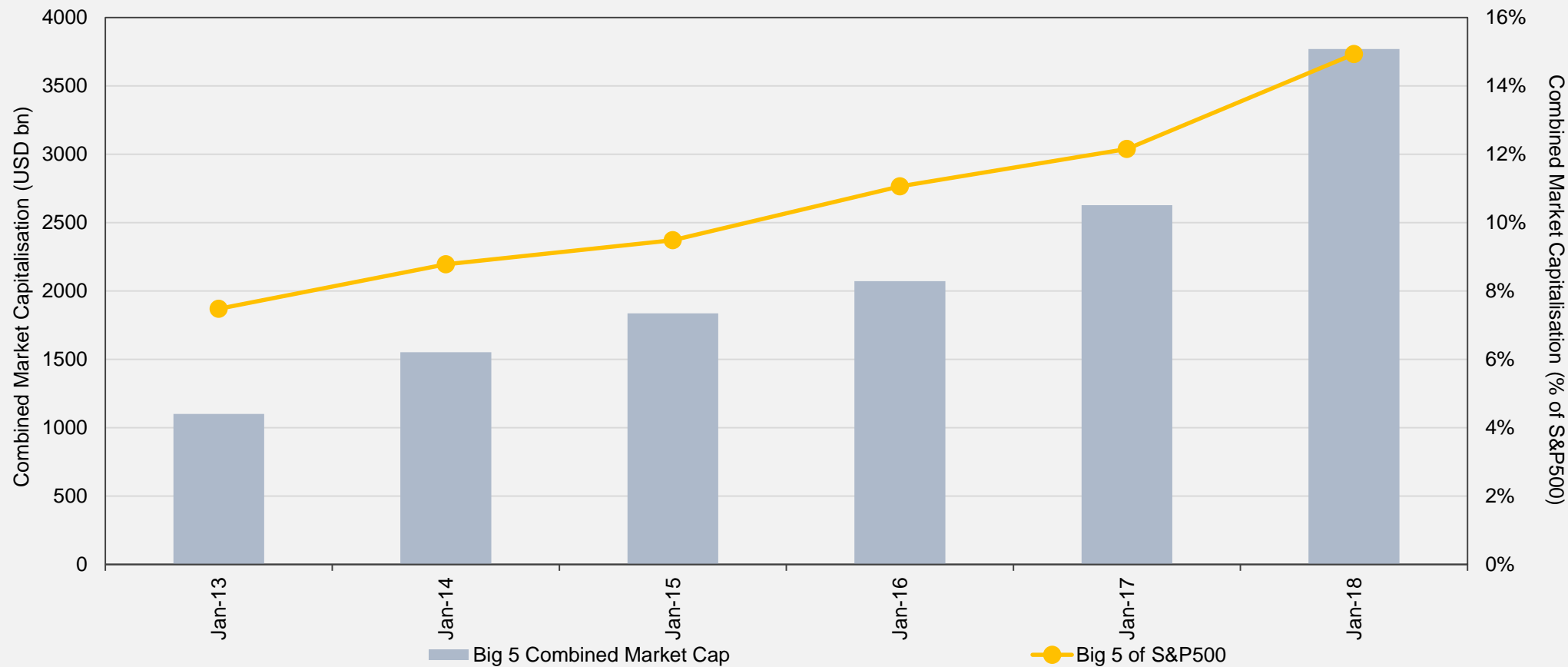


# Auscap: Financials

## Dominance of the Big 5 US technology companies

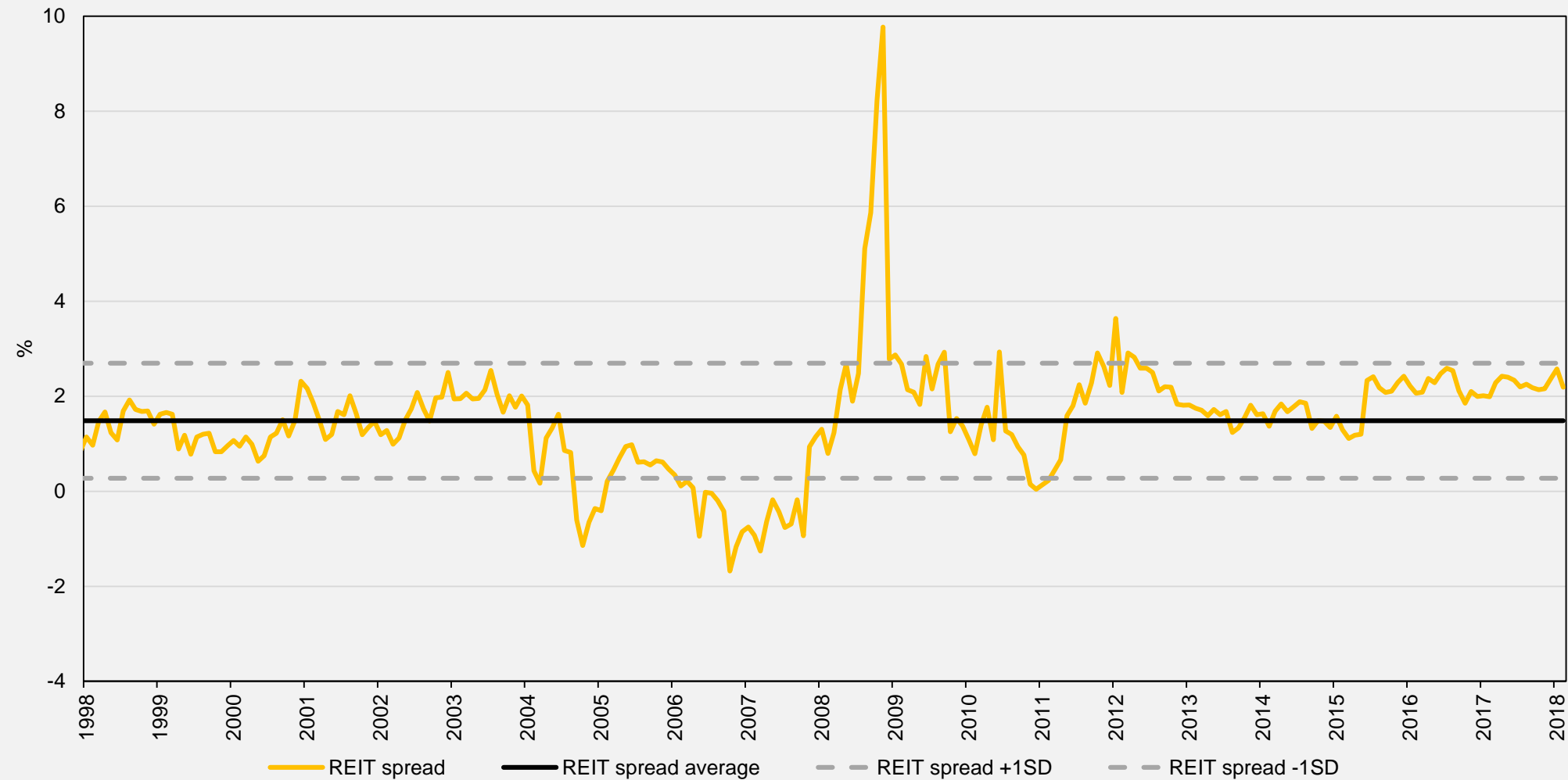
- The Big 5 are responsible for over 25% of gains over the last 5 years

### The Big 5 Dominance: AAPL, GOOGL, AMZN, MSFT, FB



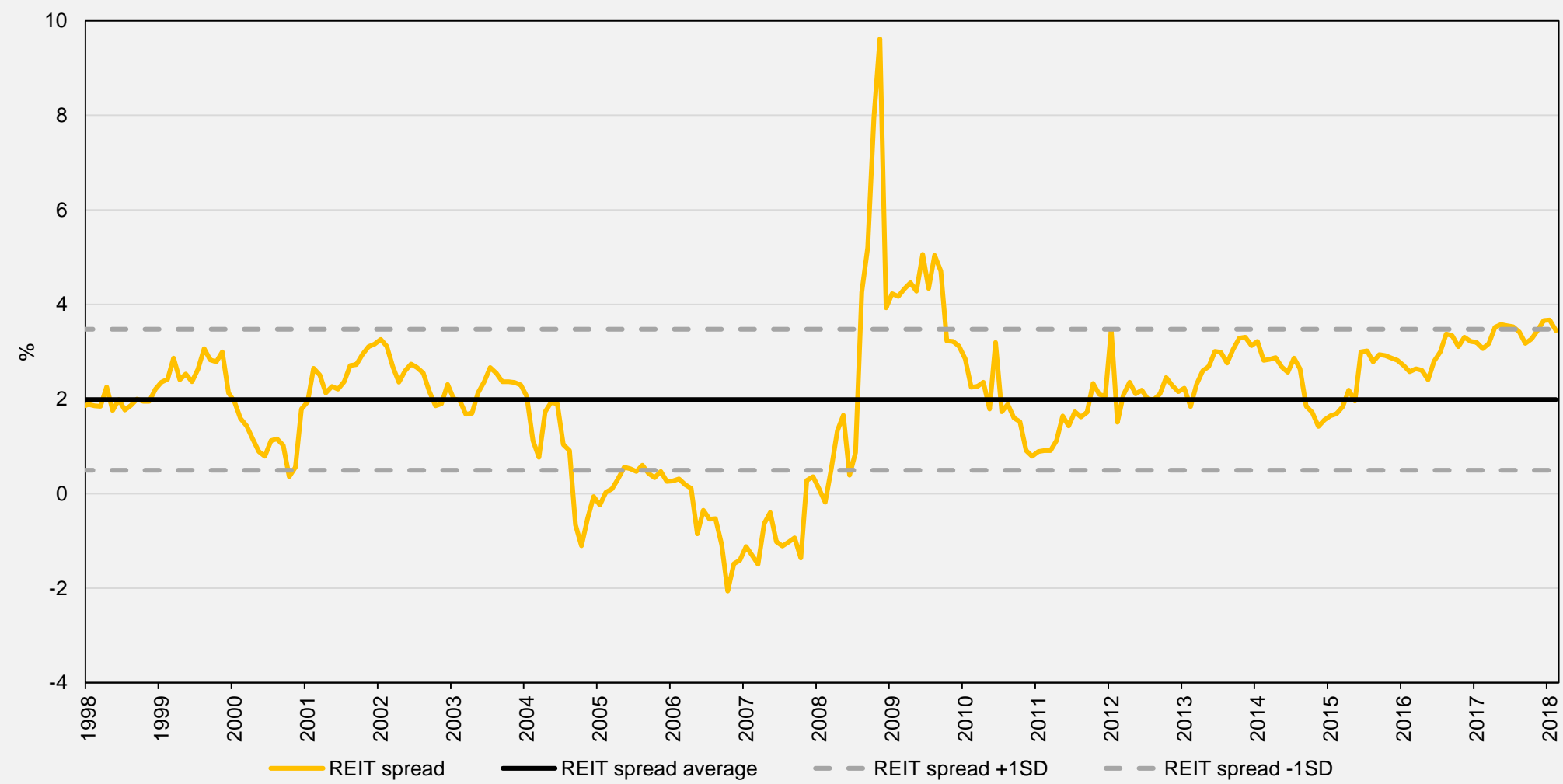
# Auscap: REITs

REIT dividend yield spread over 10 year bond rate



# Auscap: REITs

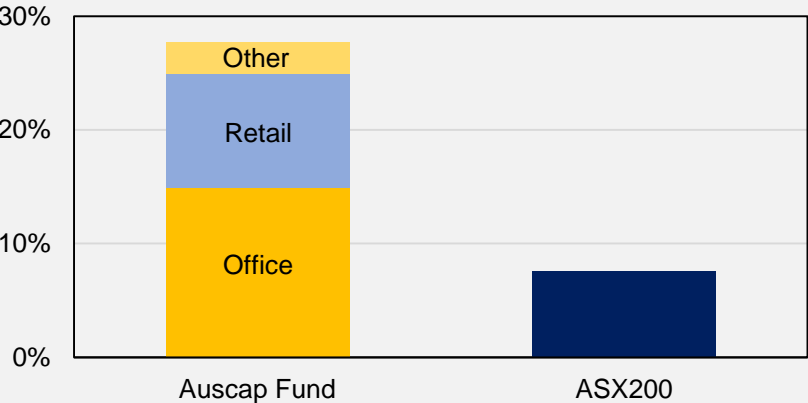
REIT dividend yield spread over RBA Cash Rate



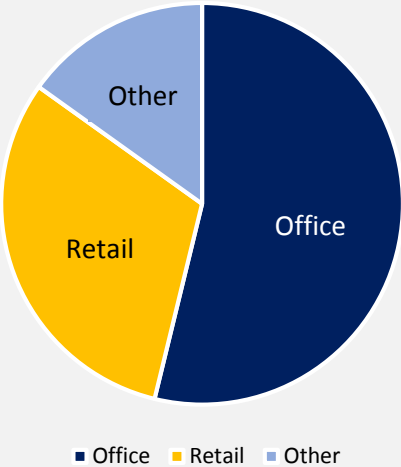


# Auscap: REITs

Current Portfolio - REITs



Auscap's REITs - April 2018



	Auscap REITs	Cash	10yr Bond
Premium (Discount to NTA)	5.1%	0.0%	0.0%
Yield	6.6%	1.5%	2.8%
Growth (p.a.)	7.7%	0.0%	0.0%
Gearing	26.2%	0.0%	0.0%
WALE	6.0 Years	-	10.0 Years



# Summary

- Value investors with a quality bias
- Focus on both capital preservation and appreciation
- Long term investors with an investment horizon of 5 years
- Zenith and Lonsec recommended
- Available on multiple platforms
- Principals co-invested in the Fund



# Fund Details

ITEM	SERIES CLASS	MONTHLY PLATFORM CLASS	DAILY PLATFORM CLASS
<b>APIR Code</b>	ASX0001AU	ASX8411AU	ASX6124AU
<b>Management fee<sup>[1]</sup></b>	1.5375% p.a.	1.5375% p.a.	1.5375% p.a.
<b>Performance fee<sup>[2]</sup></b>	15.375% p.a.	15.375% p.a.	15.375% p.a.
<b>Bid/ask spread</b>	0.2% / 0.2%	0.2% / 0.2%	0.3% / 0.3%
<b>Application</b>	Application form in PDS	Through Platforms & IDPS	Through Platforms & IDPS
<b>Minimum investment</b>	\$100,000	As determined by IDPS	As determined by IDPS
<b>Minimum additional</b>	\$50,000	As determined by IDPS	As determined by IDPS
<b>Minimum redemption</b>	\$10,000	As determined by IDPS	As determined by IDPS
<b>Valuation / Liquidity</b>	Monthly	Monthly	Daily
<b>Redemption notice</b>	1 month	1 month	Nil
<b>Distribution</b>	Annually, financial year end	Annually, financial year end	Annually, financial year end
<b>Benchmark</b>	RBA cash rate	RBA cash rate	RBA cash rate
<b>High watermark</b>	Yes, no reset	Yes, no reset	Yes, no reset
<b>Research (Fund)</b>	Zenith – Recommended Lonsec – Recommended	Zenith – Recommended Lonsec – Recommended	Zenith – Recommended Lonsec – Recommended

[1] Management Fee payable monthly for the series class and monthly platform class, and payable daily for the daily platform class. Including GST net of RITC.

[2] Performance Fee is calculated on the total gross return less expenses and management fees in excess of the RBA Cash Rate over the performance period, payable semi-annually for the series class, monthly for the monthly platform class and daily for the daily platform class. The performance fee is subject to a high water mark with respect to previous performance and includes GST net of RITC.



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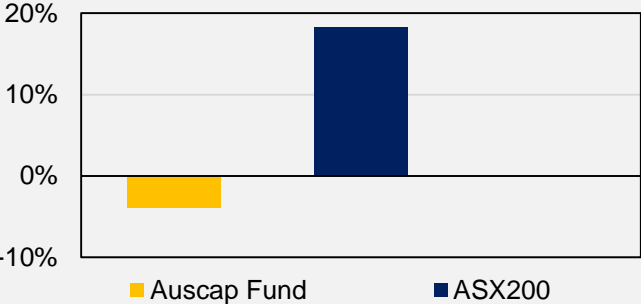
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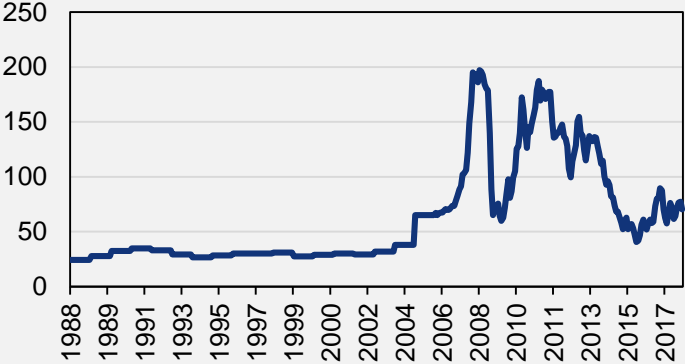


# Auscap: Materials

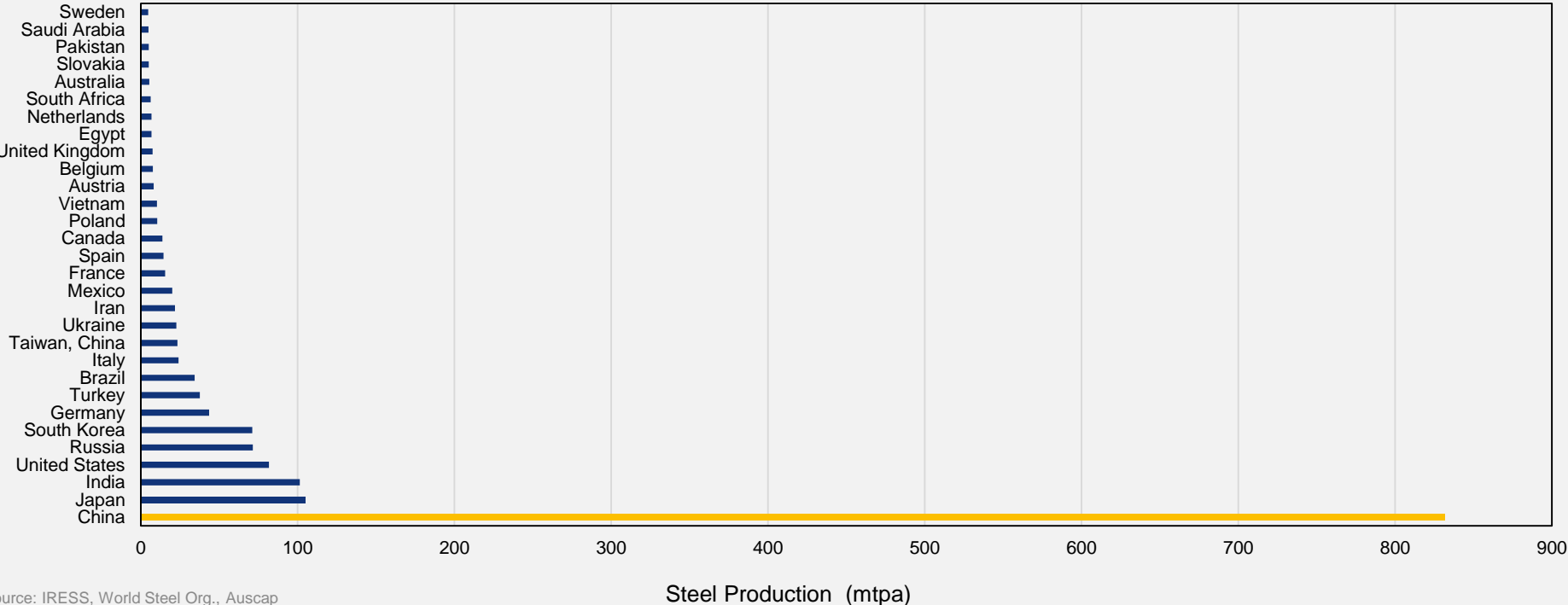
Current Portfolio - Materials



Iron Ore Price (US\$/t Fines)

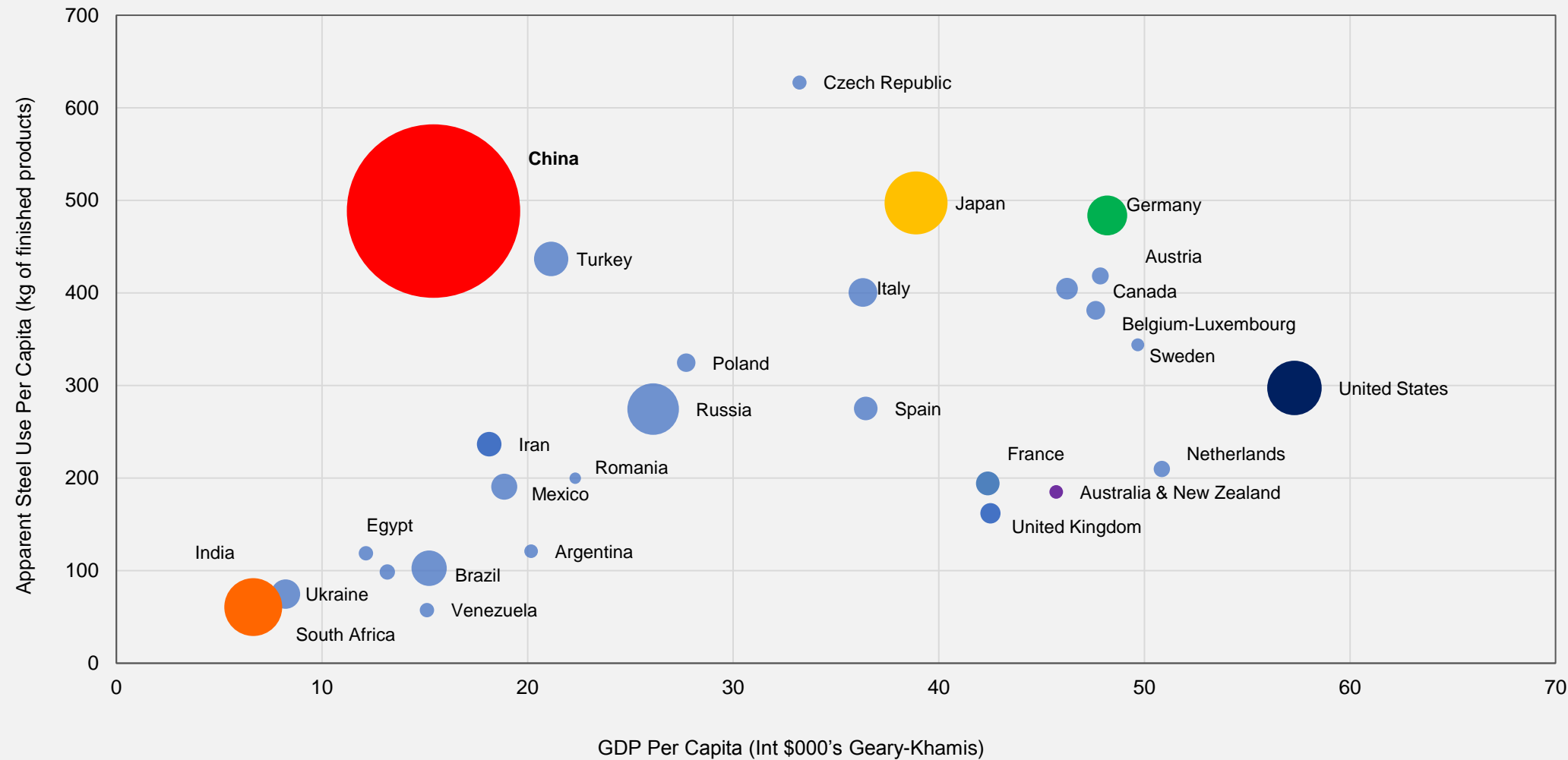


Largest Steel Producing Countries - 2017



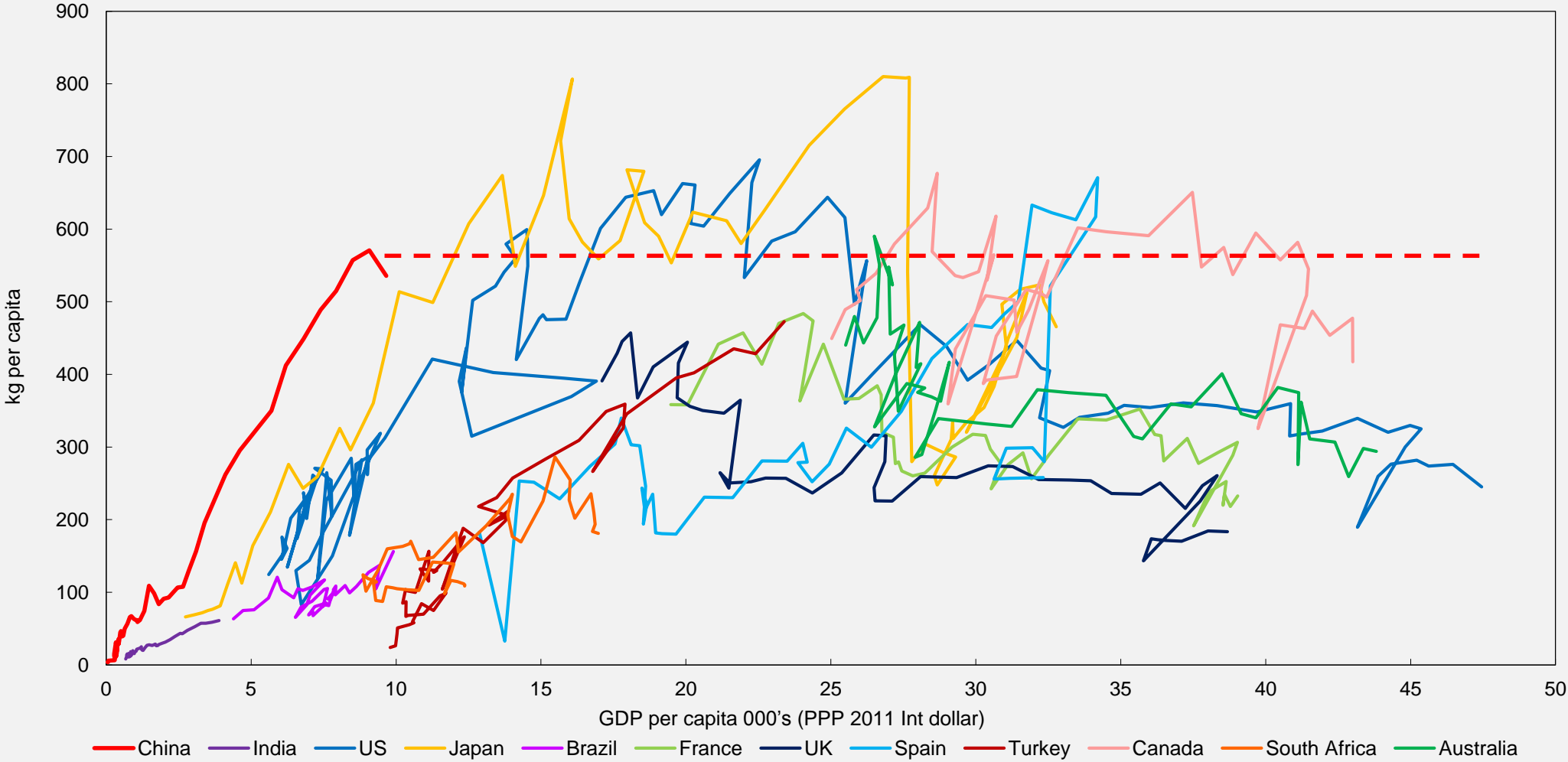
# Auscap: Materials

Steel Use vs Income Per Capita



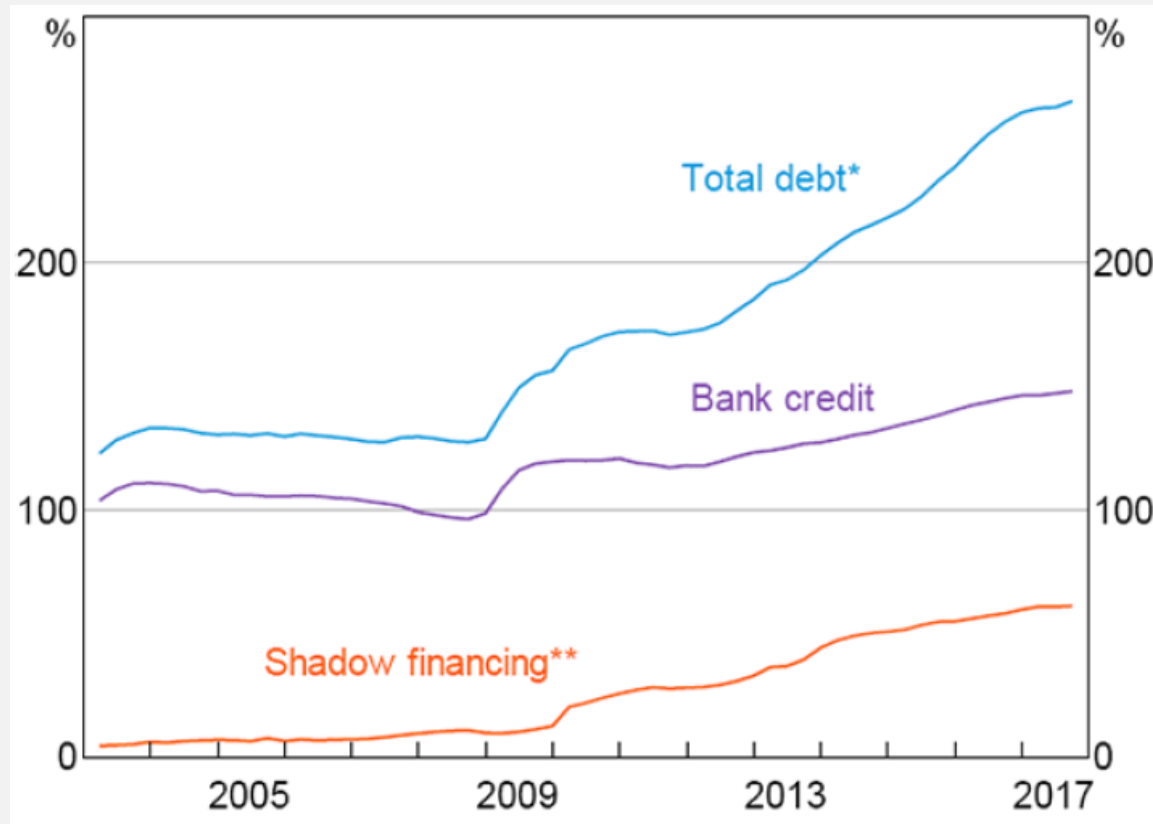
# Auscap: Materials

Crude Steel Consumption Over Time



# Auscap: Materials

China Non-Financial Sector Debt (Percent of Nominal GDP)



\*Total debt is the sum of bank credit, shadow financing, and bond financing (both corporate and public)

\*\* RBA estimate

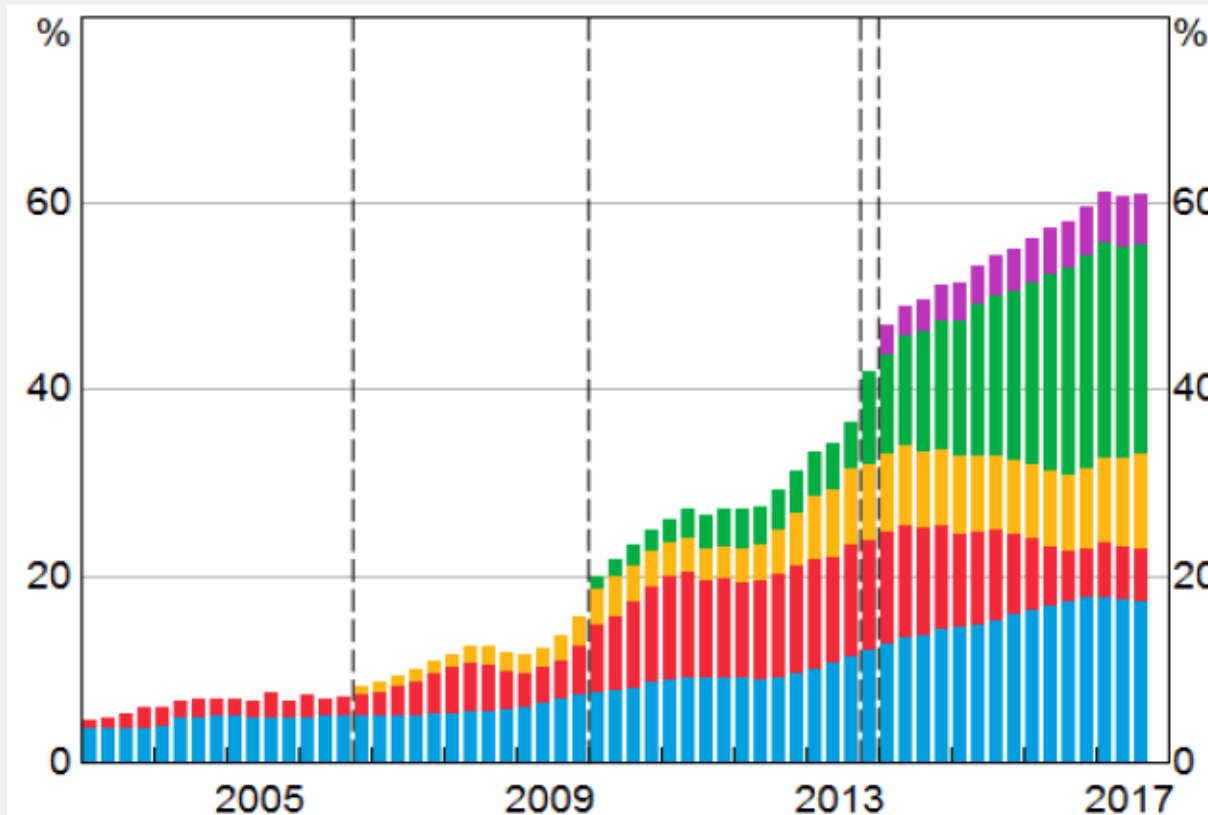
Sources: CEIC Data; RBA; Wind Information





# Auscap: Materials

China Shadow Financing\* (Percent of Nominal GDP)

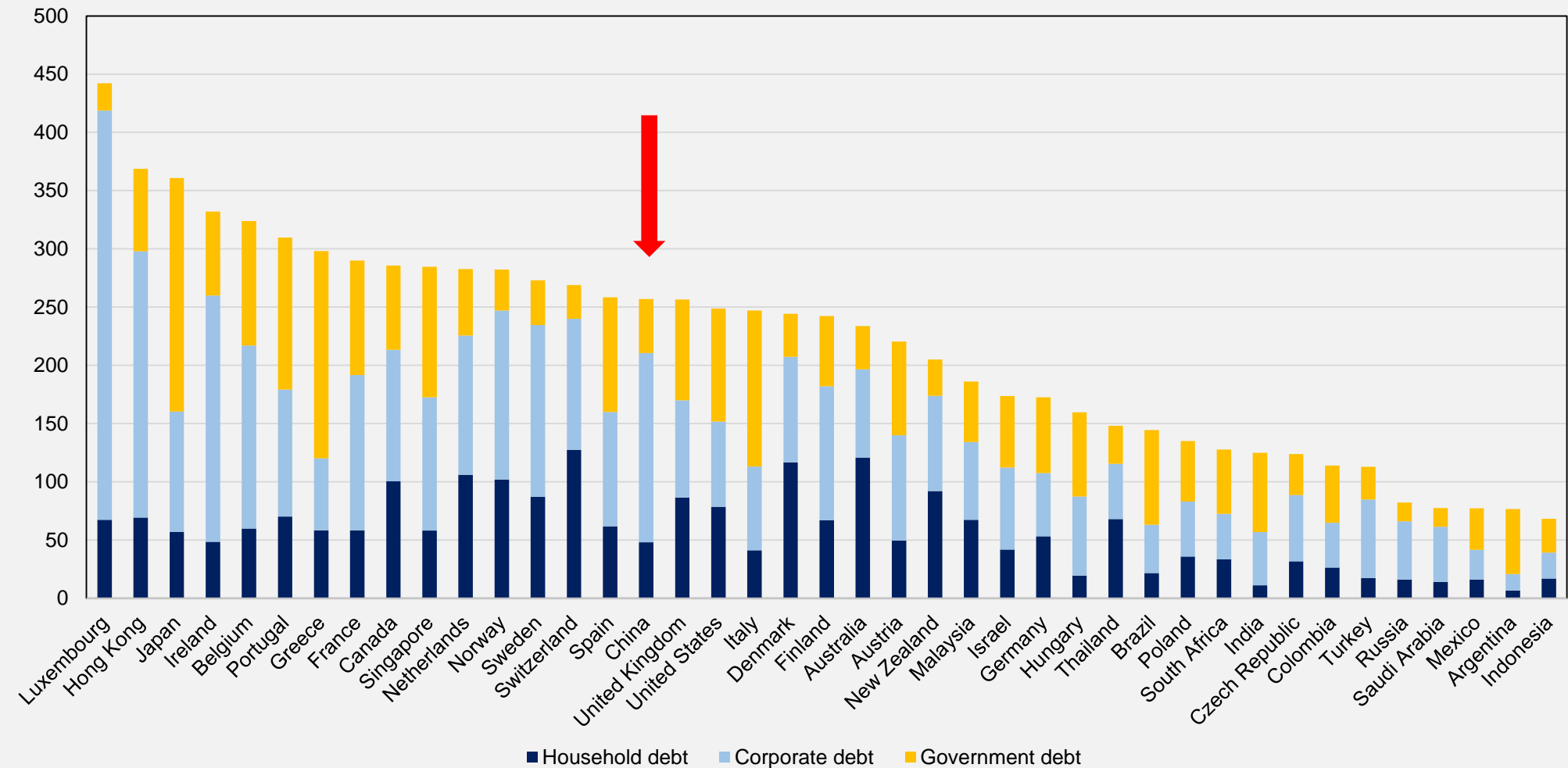


Alternative financing    Other shadow debt    Trust loans  
Bank-accepted bills    Entrusted loans



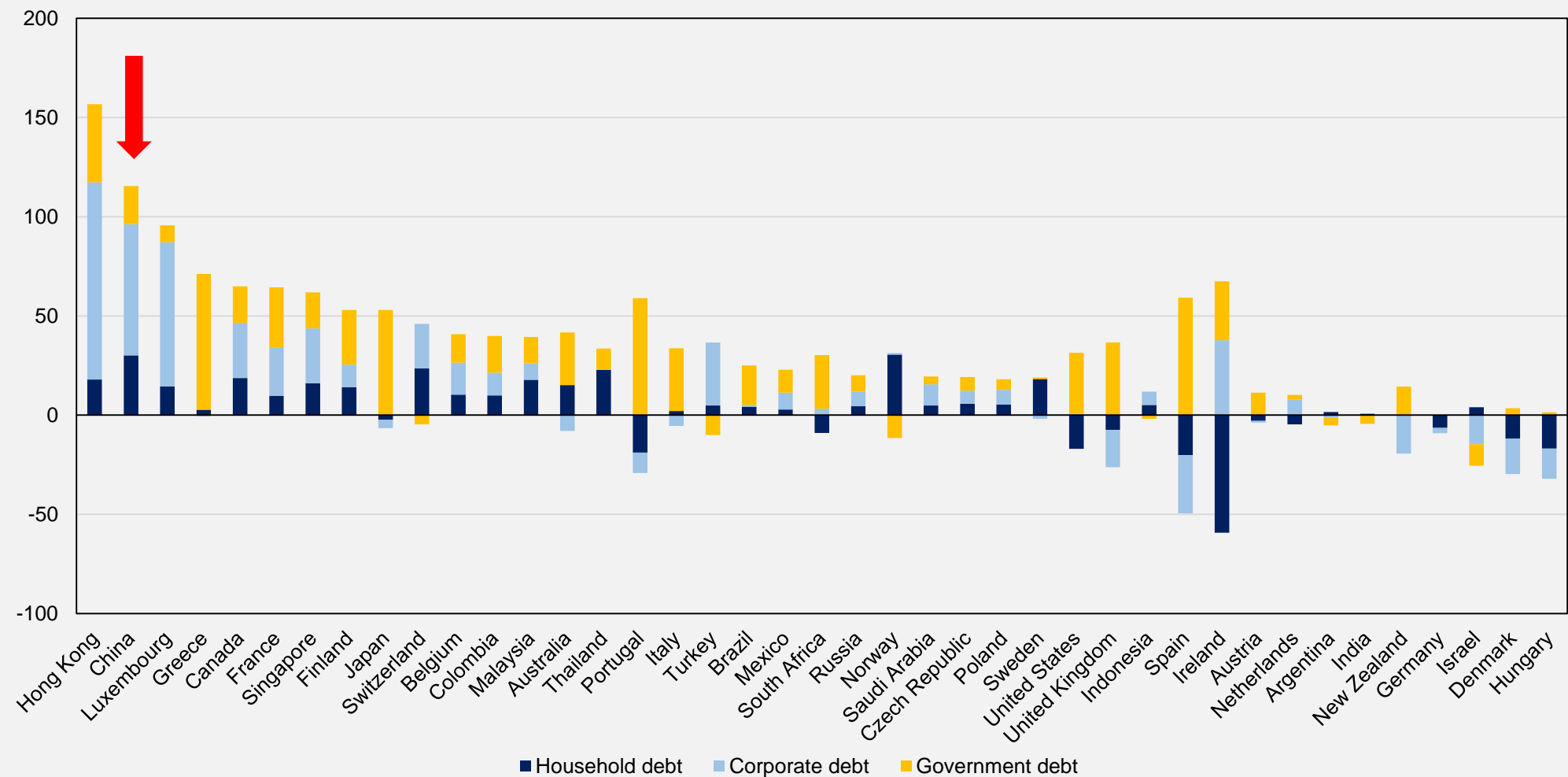
# Auscap: Materials

Total Non-Financial Sector Debt (% of GDP)



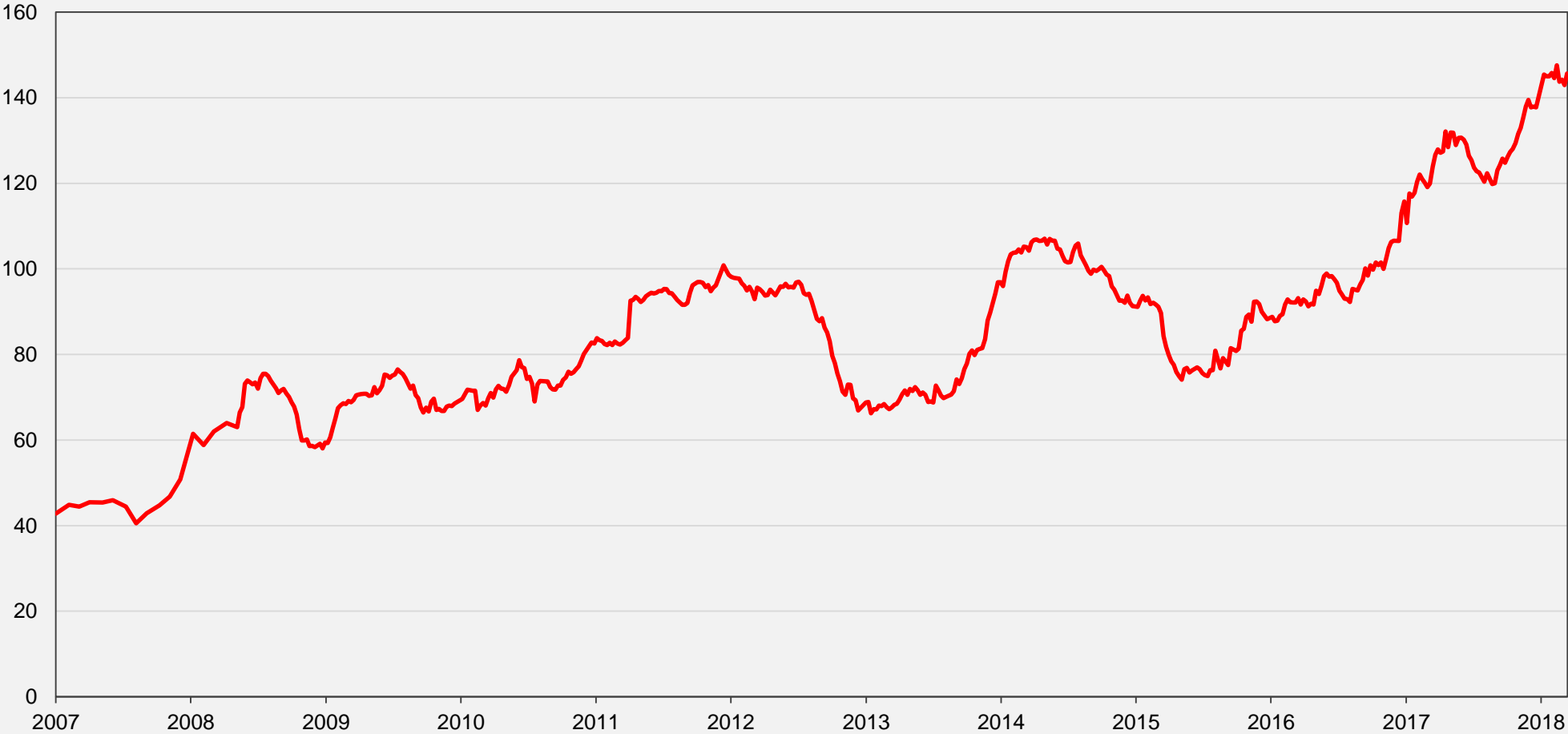
# Auscap: Materials

Change in Total Non-Financial Sector Debt (% of GDP - 2008 to 2017)



# Auscap: Materials

Chinese Port Iron Ore Inventories (million tonnes)



# Auscap: Materials

- Enough iron ore to make 19,000 Eiffel Towers



# Auscap: Materials

- Enough cars to stack from China to the moon

