



Auscap Long Short Australian Equities Fund Newsletter – November 2017

The Auscap Long Short Australian Equities Fund has been rated “Recommended” by Zenith and Lonsec. Interested wholesale and professional investors can download a copy of each report from the Auscap website www.auscapam.com.

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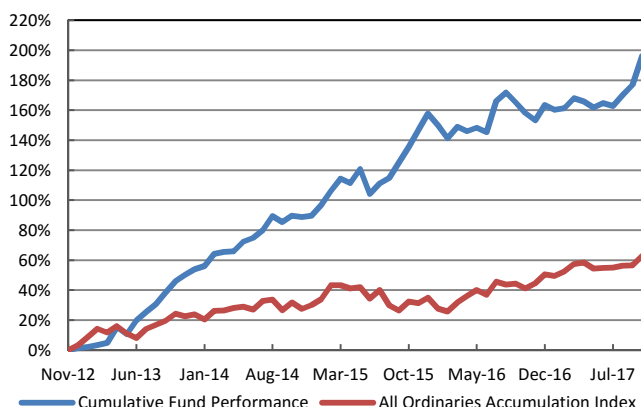
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Welcome

Welcome to the Auscap newsletter, an opportunity for us to report the performance of the Auscap Long Short Australian Equities Fund (Fund) to current and prospective investors. In each publication we will also discuss a subject that we have found interesting in our research and analysis of the market. We hope that you enjoy reading these snippets and encourage any feedback. In this edition we discuss our view on whether short term investment performance is a function of effort, manager skill and/or luck.

Fund Performance

The Fund returned 6.96% net of fees during October 2017. This compares with the All Ordinaries Accumulation Index return of 4.06%. Average gross capital employed by the Fund was 116.3% long and 4.1% short. Average net exposure over the month was 112.2%. Over the month the Fund had on average 33 long positions and 7 short positions. The Fund’s biggest stock exposures at month end were spread across the real estate, financials and consumer sectors.



Fund Returns

Period	Auscap	All Ords
October 2017	6.96%	4.06%
Financial Year to date	11.82%	5.12%
Calendar Year to date	12.41%	8.09%
Since inception	196.15%	62.77%

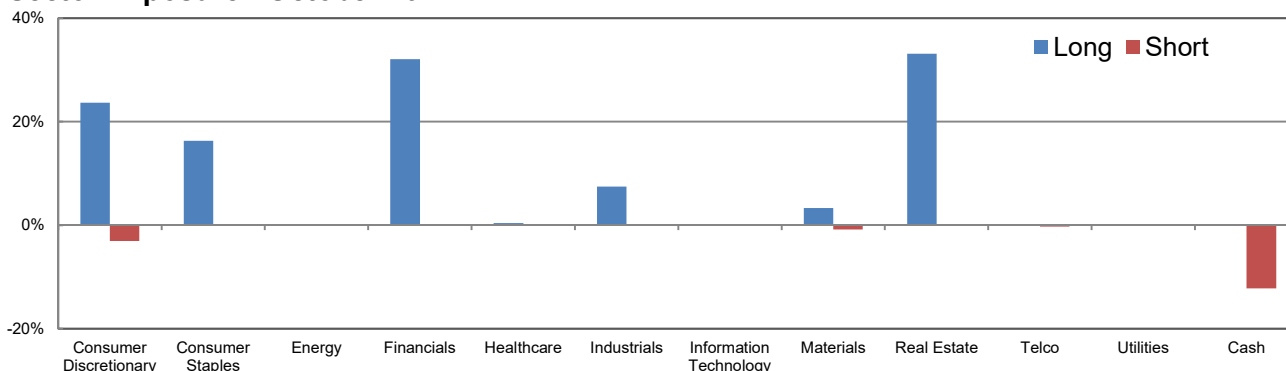
Fund Exposure

October 2017 Average	% NAV	Positions
Gross Long	116.3%	33
Gross Short	4.1%	7
Gross Total	120.4%	40
Net / Beta Adjusted Net	112.2%	78.9%

Fund Monthly Returns

Year	Jul %	Aug %	Sep %	Oct %	Nov %	Dec %	Jan %	Feb %	Mar %	Apr %	May %	Jun %	YTD
FY13						1.35	0.74	1.23	1.46	9.83	(4.05)	8.32	19.72
FY14	4.70	4.28	5.84	5.46	2.86	2.57	1.32	5.32	0.70	0.29	3.82	1.48	46.01
FY15	2.95	5.24	(2.09)	2.25	(0.43)	0.44	3.65	4.90	3.98	(1.36)	4.43	(7.55)	16.81
FY16	3.46	1.64	4.82	4.65	4.69	4.56	(3.01)	(3.54)	3.22	(1.24)	0.96	(1.19)	20.13
FY17	8.48	2.13	(2.37)	(2.72)	(1.83)	4.00	(1.20)	0.42	2.52	(0.81)	(1.53)	1.18	7.97
FY18	(0.77)	2.75	2.53	6.96									11.82

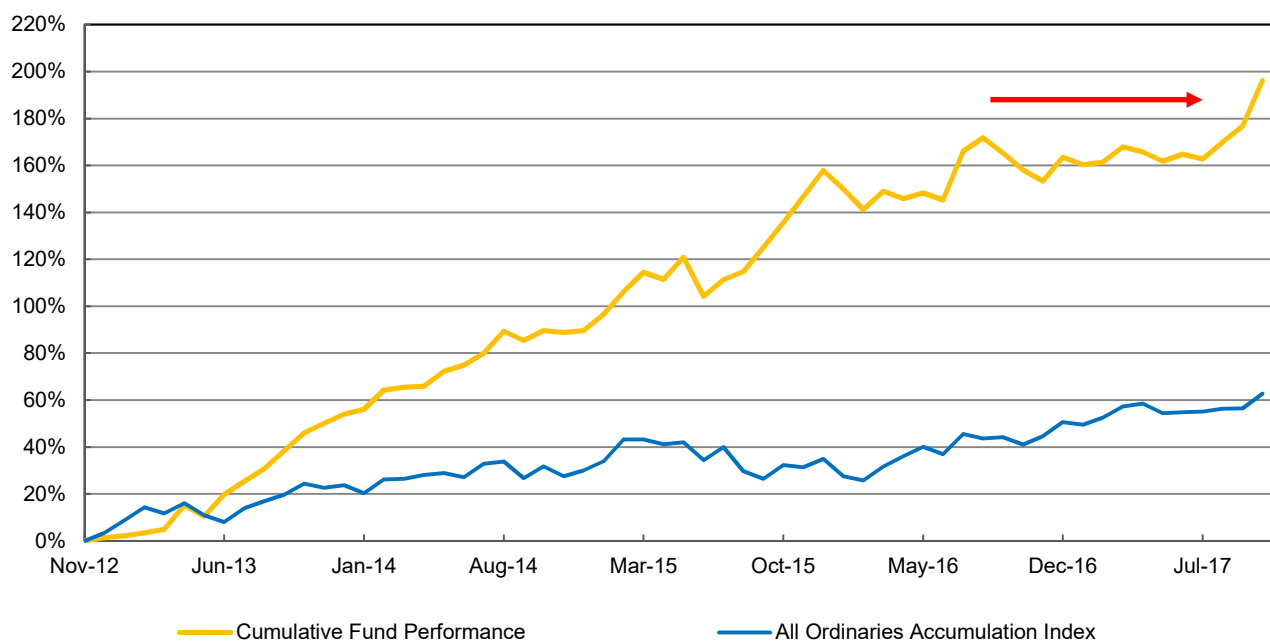
Sector Exposure - October 2017



Is effort correlated with investment performance?

The Auscap Fund has experienced a surprisingly strong last quarter. In the three months to 31 October, the Fund has delivered a compound return of 12.7% net of fees to investors. It should be added that this comes after a somewhat lacklustre twelve months where the value of the Fund's assets largely drifted sideways with the majority of the returns coming from dividends and distributions. So what has changed? What has caused the value of the portfolio to increase recently?

Auscap Performance Since Inception (Post Fees)



Our answer is that while we cannot be certain, it has most likely been driven by a change in the “perception” within the domestic investment community around some of the companies that we own. ***It has certainly had very little to do with any changes we have made in the portfolio.*** In fact, over 98% of the portfolio's return over the last three months has been derived from stocks that have been in the portfolio for more than a year. In other words, the recent performance was driven largely by investment decisions made more than a year ago. The quality of investment decisions made today might not be reflected in the Fund's performance for some time.

The weighted average duration of all holdings currently in the Fund is approximately 20 months, with a weighted average market capitalisation of nearly \$12 billion. As we state frequently, we like to buy high quality businesses that generate substantial and growing cash flow when they occasionally trade at attractive prices. This is not very often! We do not try to time the market and buy shares when we think they are going up. We look to buy stakes in operating businesses when we think they are cheap. The difference between the two is chalk and cheese.

It reminds us of an unusual characteristic of asset management. Unlike many endeavours in life, there is no immediate correlation between effort and performance. Doing a substantial amount of work finding investment opportunities today is unlikely to result in immediate investment performance success. A lot of hard work today *might* result in investment success at some point in the future, but this is not guaranteed. However, in our experience, without significant hard work it is highly unlikely that an investor will experience consistent investing success. So for the economists amongst the readership, one might say that hard work is a necessary but not sufficient condition for generating strong investment performance over time. And this is what makes investing such an intriguing exercise to the huge number of people who try their hand at it.

From Auscap's perspective, we are constantly looking for good companies to invest in. We actively follow many ASX listed companies that we believe meet the criteria for being a good business. But in our view, sensible investing also involves a careful consideration of price. We aim to be both patient and disciplined in waiting for opportunities to buy into high quality companies at prices we consider attractive. Once the purchase has been made, we look to own our share of the company for a long time. Only a change in our perception of the company or a significant and unjustified share price increase will cause us to consider reducing or exiting a high quality business bought at an attractive price.

Just when and if the market decides to reprice the companies we own is not something that we consider or can control. We spend our time focused on making sure our investment thesis is sound. That way the value of our investment will grow as the profitability and cash generation of the relevant business grows. We spend very little time focused on whether the market will value our companies appropriately today or tomorrow. We can never predict or control performance of the Fund over a short time period. Our view, as we have outlined to many of our investors, is that if we focus on the process of selecting and managing sound investments, the results over time will hopefully take care of themselves.

Over the long term, we would suggest that investment performance is a function of both manager skill and effort. But over the short term, good performance is likely to be just as much the result of luck as it is a reflection of hard work and/or manager talent. We look for investors who share Auscap's long term value-based investment philosophy and approach to managing an Australian equities portfolio. We hope to partner with these investors for many years to come.

If you do not currently receive the Auscap Newsletter automatically, we invite you to register. To register please go to the website www.auscapam.com and follow the registration link on the home page. Interested investors can download a copy of the PDS at www.auscapam.com/auscap-fund/pds. We welcome any feedback, comments or enquiries. Please direct them to info@auscapam.com.

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