Auscap Long Short Australian Equities Fund Newsletter – July 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.

Please note that the Auscap Fund's administrator, White Outsourcing Pty Ltd, has been acquired by Link Administration Holdings Limited and is now known as Link Fund Solutions.

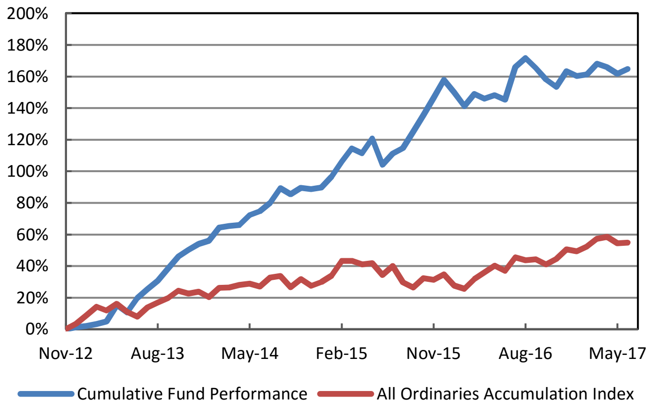
Disclaimer: This newsletter contains performance figures and information in relation to the Auscap Long Short Australian Equities Fund ARSN 615 542 213 from inception of the Fund. The actual performance for your account will be provided in your monthly statement. Actual performance may differ for investments made in different classes or at different times throughout the year. This newsletter is intended to provide general background information only. It is not a Product Disclosure Statement under the Corporations Act 2001 (Cth), nor does it constitute investment, tax, legal or any other form of advice or recommendation to be relied upon when making an investment or other decision. Past performance is not a reliable indicator of future performance. While all reasonable care has been taken to ensure that the information in this document is complete and correct, no representation or warranty is given as to the accuracy of any of the information provided, including any forecasts. To the maximum extent permitted by law, Auscap Asset Management Limited ACN 158 929 143 AFSL 428014, its related bodies corporate, directors, employees and representatives are not liable and take no responsibility for the accuracy or completeness of this document. No investment in the Fund should be made without fully reviewing the information, the disclosures and the disclaimers contained in the Product Disclosure Statement, a copy of which is available at www.auscapam.com, or any supplement to that document and obtaining investment, legal, tax and accounting advice appropriate to your circumstances. You are receiving this newsletter because we hold personal information about you, namely your contact details. You should view Auscap's Privacy Policy to understand how your personal information will be used and processed.

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 biases created by the availability and accessibility of information.

Fund Performance

The Fund returned 1.18% net of fees during June 2017. This compares with the All Ordinaries Accumulation Index return of 0.28%. Average gross capital employed by the Fund was 87.6% long and 17.8% short. Average net exposure over the month was 69.8%. Over the month the Fund had on average 27 long positions and 8 short positions. The Fund's biggest stock exposures at month end were spread across the real estate, financials and consumer discretionary sectors.



Fund Returns

Period	Auscap	All Ords
June 2017	1.18%	0.28%
Financial Year to date	7.97%	13.07%
Calendar Year to date	0.53%	2.82%
Since inception	164.85%	54.83%

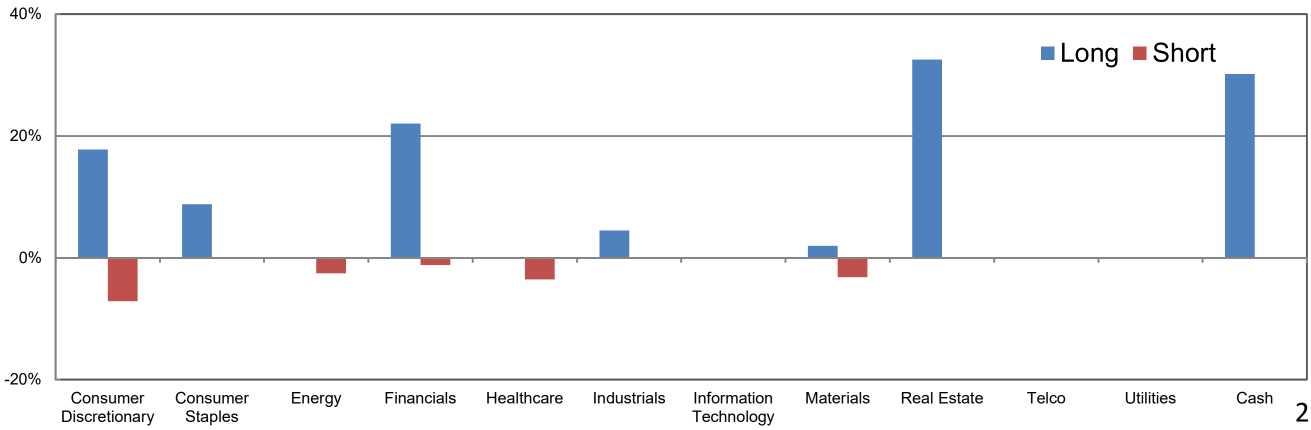
Fund Exposure

June 2017 Average	% NAV	Positions
Gross Long	87.6%	27
Gross Short	17.8%	8
Gross Total	105.4%	35
Net / Beta Adjusted Net	69.8%	31.2%

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

Sector Exposure - June 2017



You are what you read: Biases created by the availability of information

We recently attended an economics forum. The speaker was distinguished and the room full of economically informed, knowledgeable and financially literate investors and fund managers. The presenter outlined in his opening address that in his considered opinion, the greatest threat to global and domestic growth over the coming years came from financial risks building in China. Following this short opening address there was a question and answer session.

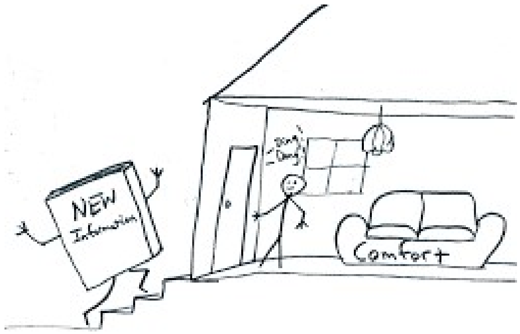
The next hour was dominated by a general discussion of the speed of interest rate hikes in the USA. There were different views within the room, but mostly the differences were marginal from an absolute standpoint, rest assured no one was arguing the case for lower rates! The conversation focused on the US Federal Reserve's "dot plot", the commentary changes in speeches by the Chair, Janet Yellen, and other various nuances, real and perceived, associated with the enormous amount of information available in relation to the US interest rate cycle. Very little discussion was had around the major risk identified by the speaker – China. The issue was raised again, but with little reliable information on China's financial conditions available the discussion was brief and so the conversation moved on. We would be surprised if many of the participants left the room thinking about financial risks within China, because it was not the focus of the session, despite being identified as the most significant issue.

The information people focus on is frequently dictated by the information that is readily available to them. But as Albert Einstein famously stated: "*Not everything that counts can be counted, and not everything that can be counted counts*."

Most investors, us included, spend considerable time focusing on data that can be analysed. People tend to focus on things that can be measured or calculated, and often ignore those things that are difficult or impossible to measure or calculate. If there is no reliable data or source of information, what is the appropriate action to take? To use the prior example, while it may be interesting to analyse the "dot plot", its importance is dwarfed by financial risks in China. By studying what is intriguing (rather than what is useful), we often exaggerate its importance in our own minds. Investors tend to focus on information that is more voluminous as opposed to more valuable.

At Auscap we *try* to spend time on things that matter, and less on things that do not. That might sound obvious, but it can be incredibly difficult to do. It is hard to focus on a risk that might be significant but is difficult to quantify or analyse. We generally believe that there is a proportional relationship between the amount of time it took someone to prepare something and its usefulness. The time, care and consideration involved in producing an autobiographical account of lessons learnt in the financial markets over one's lifetime is likely to make it more worthy of attention. Similarly the effort and strict guidelines under which an annual report is compiled indicates that it offers considerable information to the astute investor. Therefore we *try* (but do not always succeed) to spend more time on things that took longer to prepare. We believe it is more important to spend time reading books and annual reports than newspapers and websites, albeit this is difficult to do in practice. It is difficult because the latter is *designed* for consumption, with flashy photos and attention grabbing quotes and headlines, whereas the former is designed for information, to be accurate in its statements and reliable for the reader.

When investing it is important to be responsive to new information. This is also not an easy task, particularly if the new information challenges previously held assumptions. This is actually where it is most important to consider the information, particularly when the new information challenges established wisdom. We want to make sure that we are open to changing our perspective. As John Maynard Keynes stated "*the difficulty lies not so much in developing new ideas as in escaping from old ones*".



As human beings we rarely interpret numerical information from within an "absolute" framework. We look for reference points and calculate the value of one thing *relative* to another. It is rare for an analyst to declare that stock A is expensive if its peers, stocks B, C and D, are trading at considerably higher multiples of their earnings, even if all four are mispricing risk relative to likely return. Similarly, it is unusual for an analyst to declare a whole sector cheap, because if the sector is cheap conventional wisdom would suggest it must be cheap for a reason. Investors rely on the rationality of their peers, but this is a somewhat circular argument. At the extremes there are huge numbers of stocks, often whole sectors, that are simply cheap or expensive.

We try to avoid this trap by looking at new companies without any reference points. We do not look up their market capitalisation, enterprise value or valuation multiples. We should be familiar enough with different risks and required rates of return to appropriately value a business without the need for a huge spreadsheet of comparable companies and their valuation metrics. We analyse the company's filings and annual reports and attempt to arrive at a view of what a fair valuation might be. Then we compare our estimate with the actual market capitalisation. Bargains can be had when our estimate of value is significantly higher than the current market capitalisation. Mostly it is the other way around. But the independence of thought is important. In this way we try to minimise the effect of some of our cognitive biases. That our opinions can be shaped by information we are already aware of that appears on first glance to have some bearing on our valuation of an asset, but really only constitutes a data point worthy of consideration *after* independent evaluation has occurred. In this way we hope to take advantage of the rare opportunities the market affords us as investors to buy companies well below our view of their true intrinsic value.

If you do not currently receive the Auscap Newsletter automatically, we invite you to register. To register please go to the website http://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.

Auscap Asset Management Limited

ACN 158 929 143 AFSL 428014
Lvl 30, 9 Castlereagh St, Sydney

Email: info@auscapam.com
Web: www.auscapam.com

Service Providers

Prime Brokerage: Citi Global Markets
Administration: Link Fund Solutions

Tax & Audit: Ernst & Young
Legal: Henry Davis York