Auscap Long Short Australian Equities Fund

Newsletter – April 2019

Fund Performance*

Period	Auscap	All Ords
March 2019	3.1%	0.7%
Financial Year To Date	(11.4%)	2.9%
Since Inception	164.7%	81.2%
Annualised Returns	16.6%	9.8%

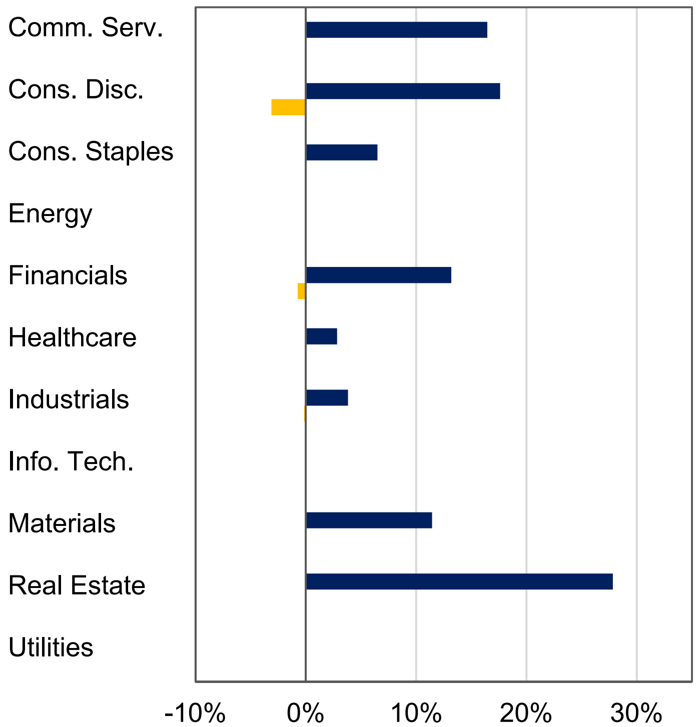
Fund Exposures

March 2019 Average	% NAV	Positions
Gross Long	99.7%	34
Gross Short	4.1%	9
Gross Total	103.8%	43
Net / Beta Adjusted Net	95.6%	80.7%

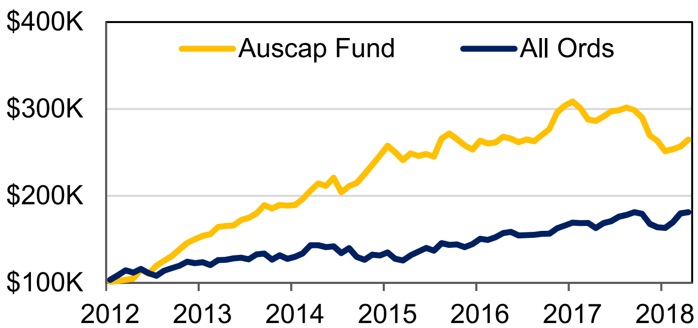
Portfolio Commentary

The Fund returned 3.1% net of fees during March 2019. This compares with the All Ordinaries Accumulation Index return of 0.7%. Average gross capital employed by the Fund was 99.7% long and 4.1% short. Average net exposure over the month was 95.6%. Over the month the Fund had on average 34 long positions and 9 short positions. The Fund's biggest stock exposures at month end were spread across communication services, consumer, financials, materials and real estate sectors.

Sector Exposure - March 2019



Fund Performance*



Fund Financial Year Returns*

FY	%	FY	%
FY13	19.7%	FY17	8.0%
FY14	46.0%	FY18	12.7%
FY15	16.8%	FY19	(11.4%)
FY16	20.1%	CY19	5.3%

Top 10 Investments

Adelaide Brighton	JB Hi-Fi
Blackmores	Mineral Resources
Centuria Metropolitan REIT	Nine Entertainment
CYBG	Super Retail Group
GDI Property Group	Unibail-Rodamco-Westfield

** Performance figures are calculated for the lead series net of all fees and expenses assuming the reinvestment of all distributions. Past performance is not a reliable indicator of future performance.*
^ Top 10 long investments in alphabetical order as at 31 March 2019.

A Long Term Approach To Investment

To suggest that investing in equities can be challenging is an understatement. Whether you are investing directly into individual stocks or investing in a managed fund where a professional investor makes those decisions on your behalf, having exposure to equities can be a mentally and emotionally taxing exercise. It would seem that human beings are not naturally wired to be great investors. Investing involves making informed and rational decisions to buy into companies knowing that the results these companies will deliver is uncertain and subject to an unknowable future. Furthermore, changes to that environment frequently result in disproportionate moves in the valuations ascribed by the market to these listed companies. A small change in expectations for future profitability can often have an outsized impact on a company's share price, largely because of the human reaction or emotional response to the change. Investors compound the expected change in profitability with higher enthusiasm or increased pessimism towards its valuation.

How can one sensibly invest in such an environment?

Some investors choose an approach that sees them trading in and out of stocks quickly. Their portfolios might look very different one month to the next. They often sell the stocks where the news has become incrementally negative and buy the stocks where the news has been positive. This approach requires them to act quickly and, taken in aggregate, is typically responsible for the outsized reactions described above. We think of this approach as being the "poker approach" to investing. If you decide you do not like your current hand, discard it and wait for the next round of cards, they will be entirely different to the ones you just held. While it might be the right approach in poker, it has never felt to us like the right approach to investing. It requires an investor to have superior foresight, better interpretation of data and a faster reaction to newsflow than their competitors. Achieving consistency in this regard is logically impossible. It also requires a significant amount of knowledge of an unusually large number of companies. Changing a portfolio of investments on a regular basis, even assuming sufficient liquidity and ignoring the impact of transaction costs, would require an investor to regularly and quickly attain sufficient knowledge across a range of new companies in unfamiliar industries, a daunting and likely unrepeatable strategy.

Conversely, we take a long term approach to investing. We identify the business attributes that we think will make for a good long term investment. These include a simple, proven business model, strong cash generation, a track record of attractive return on invested capital, growth opportunities for investing future capital, a sensible balance sheet, products or services that we are familiar with and a management team we trust. We then have patience with these investments, both in purchasing them initially and then holding them on an ongoing basis, recognising that there will be periods when they are out of favour with the market, in many instances without regard to company performance. In our experience these periods are outweighed by the results delivered over time from companies that have these superior attributes.

Opportunities for outperformance

Ironically the exact conditions described in the opening paragraph create the preconditions for new opportunities and generating long term investment outperformance. Buying high quality businesses that we plan to own for a long time when they are trading at attractive prices is the fundamental basis of Auscap's investment philosophy. These prices are typically found when sentiment is poor, when investors are steering clear of an entire sector because of short term or macroeconomic concerns, and/or when fear is dominant despite low market expectations. Investing is one area in which very few people swoop in and buy aggressively when stocks are on sale. And while we are prone to the same emotional influences, we focus heavily on the facts to make decisions. Rational decision making is critical to long term performance and we are always looking to buy good companies when they are cheap. We are excited by some of the opportunities the market has presented in recent months.

Our approach to long term investing

What is the right approach to take when circumstances change resulting in a period of poor overall performance for an investor, even a professional investor? We always take the same approach. We first focus on a re-evaluation of the facts, often cross referencing hard data with on-the-ground feedback and anecdotal evidence. If the facts have changed it is important that we reassess the investment. The corollary to this is that in many instances the facts will not have changed materially and stock price declines are reflecting a significant change in sentiment towards the company or companies in question. As the father of value investing, Benjamin Graham, stated *"in the short run, the market is a voting machine but in the long run, it is a weighing machine"*. And the thing being weighed in the long run is earnings.

It should be no surprise then that some of the significant detractors from the Fund in periods when performance has been negative have also been some of the Fund's most significant positive contributors in aggregate over its lifetime. We expect that many of these businesses will continue to be strong contributors for the Fund's investors in the future. This investment approach in a relatively concentrated portfolio will always have ebbs and flows in the short term, but from our perspective it is the only approach that makes sense to generate long term compounding returns for our investors.

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