

ARCO Investment Management

ARCO Absolute Trust

Monthly report: January 2019

No Christmas rally in December which brought to a close the toughest calendar year for equity returns since 2011. The gold price rallied, yield curves flattened, local credit conditions deteriorated further, looming deadlines for geo-political events – volatility to rise into 2019.

Performance	Month	Qtr	1 Year	3Yr(pa)	Life (pa)
Fund return (net)	0.00%	-2.42%	-6.51%	2.34%	7.02%
Positive months			33%	64%	76%
Worst month					(3.2%)
Volatility					4.0%
Sharpe ratio					0.8

note

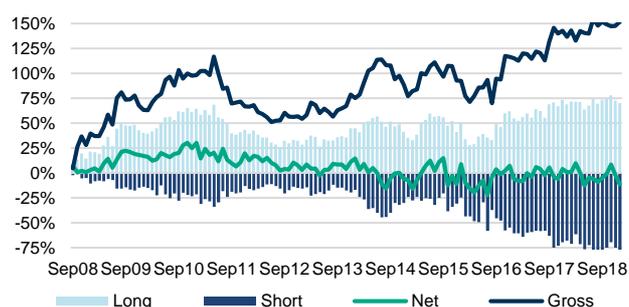
Monthly key contributors – by sector

Longs	30 positions
Positive	Gaming, media, transport
Negative	Resources
Shorts	19 positions
Positive	Banks, healthcare
Negative	Index futures, REITs, retail

Cumulative performance



Fund investment profile (% NAV)



Portfolio settings

% of NAV	Long	Short
Equities	70.2%	-44.6%
Debt/ Hybrids	0%	0%
Derivatives		-37.0%
Gross exposure		151.8%
Net exposure		-11.4%
Concentration by position	Long	Short
Top 5	25.11%	(19.89%)
Top 10	40.58%	(32.02%)
Top 15	52.88%	(40.40%)

Fund strategy and outlook

The Trust's objective is to steadily compound investor returns over time through stock alpha generation, with an overarching focus on capital preservation.

The Trust recorded a net return of 0.0% for the month.

Central bank sentiment turned suddenly dovish, market volatility eased and global equities rose significantly in January with the MSCI World Index rising 7.8% - its largest monthly rally since Oct 2011. The ASX rallied a more modest 3.7% for the month, with positive contributions from all sectors, other than financials – a short-lived pause as it too rallied strongly post the RC report release in early Feb.

The about-turn from Central banks was a key focus point for equity markets during the month. Investor emphasis was squarely on the return of the "central bank put", with much less interest on the causes of this change in policy direction, which seem to centre on much weaker global growth, and a reassessment of economic risk factors. Fresh on the heels of the Federal Reserve's capitulation came the RBA's shift to neutral interest rate guidance, with cuts to its GDP growth outlook. Quite how the RBA reconciles its concerns over the impact of falling house prices and weak income growth on consumer expenditure with 3% GDP growth is unclear to us. With A\$10-year bond yields now at 2.10%, it's clear that fixed income investors are looking at an emptying glass.

It's just this issue that remains key for markets. Coupon-facing investors fear being placed back on a starvation diet. Recent equity market weakness did lead to better value for some stocks of interest to us, though valuations in absolute terms are not cheap, and the RBA's position now expressly recognises elevated earnings risk in the domestic economy.

Throughout the month, we retained our cautious view of the local equity market, maintaining flat to slightly negative net market exposure. This impacted the Trust's performance, as substantial gains made across our long holdings were offset by losses in the short portfolio. As the market rallied during the month and leading into February's company reporting season, we acted to reduce the Trust's net market exposure by month-end.

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Performance review

The Trust delivered a flat return in January. The size and pace of the market rebound surprised us, and the Trust's cautious portfolio risk settings allowed for limited participation in a broad-based rally.

As the market rallied, the vast majority of the long holdings performed strongly, up over 5% in aggregate for the month, led most notably by Aristocrat, Tabcorp and Worley. NEC was also a relatively strong contributor, after a poor December.

The Trust's short portfolio remains tilted towards financials, housing, and property stocks. These positions were also favourable contributors to January's result, but have negatively impacted performance early in February, with the further decline in bond yields and a 'less-bad' than feared outcome in the Royal Commission final report – although the damage on credit creation (and demand) continues to unfold, in our view.

Index futures exposure, rising iron ore prices and further gains in the REITs sector also impacted the Trust's performance from the short portfolio.

February's company earnings results will provide a key temperature check on the domestic economy, and the season will be as much one of avoiding earnings 'bombs' as picking winners.

ARCO Absolute Trust – monthly returns

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FY
FY19	(0.45%)	(2.73%)	1.30%	(0.68%)	0.79%	(3.20%)	0.00%						
FY18	0.24%	(0.29%)	2.79%	1.08%	1.57%	1.76%	0.91%	(1.16%)	1.39%	(0.54%)	(0.65%)	(0.67%)	6.53%
FY17	(2.28%)	0.02%	0.56%	0.35%	0.95%	0.29%	(1.00%)	(0.98%)	0.94%	0.07%	0.17%	1.88%	0.93%
FY16	0.31%	1.52%	1.79%	1.42%	1.01%	(0.11%)	0.02%	0.77%	2.34%	(0.69%)	2.29%	0.11%	11.21%
FY15	1.03%	0.06%	0.64%	(0.71%)	(0.53%)	(1.53%)	(1.88%)	(0.08%)	0.98%	1.96%	2.04%	(1.09%)	0.80%
FY14	0.36%	0.14%	0.43%	0.32%	(0.52)%	0.54%	0.57%	1.06%	0.04%	0.57%	1.38%	0.63%	5.64%
FY13	(0.54)%	0.26%	0.29%	0.37%	0.57%	0.66%	0.46%	(0.50)%	(0.06)%	(0.70)%	1.22%	(0.18)%	1.86%
FY12	1.69%	0.29%	0.29%	0.97%	1.63%	(0.09)%	1.51%	1.03%	0.46%	0.46%	0.00%	(0.60)%	7.88%
FY11	2.34%	0.36%	1.45%	2.23%	1.66%	0.86%	1.36%	1.26%	0.50%	0.74%	0.57%	(1.38)%	12.57%
FY10	4.00%	3.88%	2.00%	2.68%	0.78%	0.09%	0.17%	0.52%	0.68%	1.45%	0.59%	0.57%	18.75%
FY09			0.67%	0.59%	2.19%	1.47%	1.81%	(0.56)%	3.10%	1.37%	2.43%	0.09%	13.90%

Note: returns are net of all fees and assume reinvestment of distributions. Fund inception date is 15/09/08. FY returns are compound returns over the stated period.

ARCO Absolute Trust – distribution history

Y/e June	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Series 1 units	\$1.23	\$1.31	\$2.03	\$0.41	\$0.12	\$0.34	\$0.46	\$0.71	\$0.43	\$0.93

Fund facts

Initial series NAV	\$9.778
Strategy	Long-short Australian equities
Objective	Positive returns in all market conditions. Overarching focus on capital protection
Firm AUM	\$138m

Distribution frequency	Yearly (bi-yearly in FY 2016)
Minimum investment	Wholesale investors only, \$100k
APIR Code	OPT0001AU
ISIN	AU60OPT0014
Fund Inception	15/9/08 (@ \$10.00 per unit)

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