

ARCO Investment Management

ARCO Benchmark Independent Fund

Monthly report: November 2017

November was another good month for equities both locally and offshore. Company earnings growth and fiscal policy drive US equities higher. The 2018 growth outlook for our equity market isn't so compelling and company fundamentals will likely matter more for stock prices.

Another US sugar-hit (tax reform)

Strong Fund alpha generation

Volatility coming back?

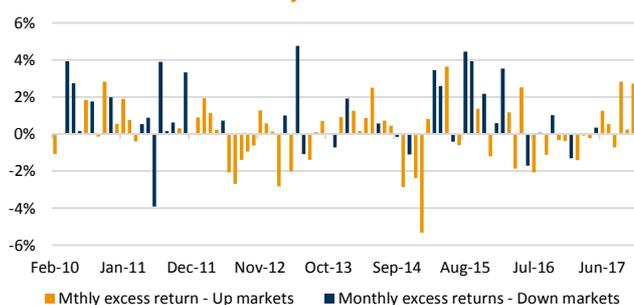
	Month	Qtr	1 Year	3 Year	Life (p.a.)
Price NAV	1.1695				
Fund (a)	4.41%	12.0%	18.9%	15.5%	13.7%
ASX300 Accum	1.69%	5.8%	14.6%	8.6%	7.3%

(a) Returns from the long portfolio of the ARCO Absolute Trust to Jun 16; actual Fund returns thereafter.

Monthly attribution and top active investments

Attribution	
Positive	Resources, retail, non-bank financials
Negative	Telecom, media
Top Active	
	O/w - CYB, WOW, JHG, AHG U/w - WBC, ANZ, NAB, BHP

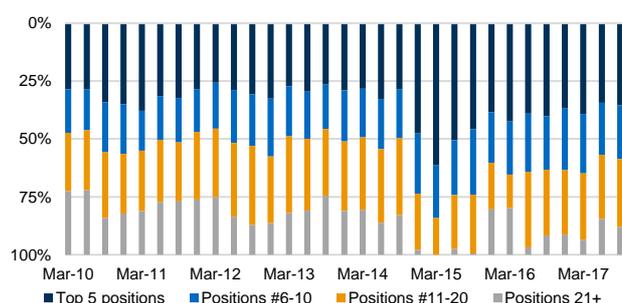
Performance: monthly excess returns



Sector weightings

	ASX300	OBIF	Active
Consumer discretionary	4.8%	7.8%	3.0%
Consumer staples	7.3%	8.5%	1.1%
Energy	4.6%	5.9%	1.3%
Financials	36.4%	31.2%	-5.2%
Healthcare	7.1%	0.0%	-7.1%
Industrials	7.4%	7.0%	-0.5%
IT	1.9%	7.5%	5.7%
Materials	17.0%	15.4%	-1.5%
Real Estate	8.2%	8.7%	0.6%
Telecommunications	3.0%	8.0%	5.0%
Utilities	2.1%	0.0%	-2.1%

Stock concentration - % of equity exposure



Fund strategy and outlook

The ARCO Benchmark Independent Fund aims to deliver investors consistent growth over time, with a strong focus on capital preservation and low downside capture.

The ASX 200 price index cracked the 6000 mark in November, reaching its highest level since early 2008. Offshore equity markets (developed countries) performed broadly on par with our local market (in AUD terms), with the notable exception of the US market which started the month trading flat until it received yet another sugar-hit on the proposed tax reform package and rose over 3% to another record high. We've been here before!

There was no such fiscal support for the Australian market and the RBA again left its benchmark rate on hold, although expressing a desire to raise once wage growth and inflation provide a stronger basis for normalisation. This still looks some way off. Long bond rates eased on these sentiments, further supporting equity flows. Unfortunately, the only major announcement from our Government was of the 'Royal Commission we had to have' which increased the headwinds already blowing through this sector, with contagion risks into other sectors.

Looking forward, we are mindful that December is traditionally a positive month for equities but our focus is always beyond one month. Into 2018, we believe that the 'lower for longer' monetary policy of central banks will continue to be unwound and that the economic fundamentals of companies will play a greater role in their stock price valuations – as they should. Corporate Australia will continue to benefit from low domestic rates which should fuel their growth plans, though consumer weakness (indebtedness and sentiment), tightening bank credit and lack of political leadership will be a challenge to broad market earnings. Volatility in our market will likely rise.

This strategy continues to focus on minimising investor draw-downs whilst compounding their returns over the long-term.

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Performance review

The Fund posted a +4.4% return for November, significantly outpacing the broader equity market.

With the local market rising broadly across most sectors in November, the long positions in the fund drove its positive return, most notably from a number of long-held positions in JHG, WOW, CYB, AHG and ORE.

Limiting the Fund's bank exposure to CBA (the only major bank that was higher in November), Macquarie and CYB was also a positive contributor to returns, with the Royal Commission announcement into banks driving further headwinds through the sector.

The market's continued re-rating of Orocobre (ORE) and Pilbara Minerals (PLS) pushed their stock prices to the very upper edge of our fair value ranges. We exited PLS and trimmed ORE, although we remain vitally interested in both investment and short opportunities around the dislocative industry change associated with EV and energy storage.

We added to our exposure in Lynas Corporation (LYC) during the month, which we view as holding a highly strategic (and cash-generative) position in the rare earth market, although we expect the recent retracement in the underlying commodity prices to continue.

The Fund has generated strong returns from FXJ, and we exited our investment in the final week prior to the spin-out of Domain Group, as the 'easy' part of the re-rate is done for the time being, in our judgement. The Fund continues to be active in TLS, where we believe a solid long investment case is emerging, amidst the very competitive state of the market and the debacle that is the NBN.

Exiting a number of stocks during the month provided an opportunity to add to a number of positions where we can find greater value including Lynas, Westfield and Suncorp.

Performance summary

	Qtr	1 Yr	3 Yrs	5 Yrs
Returns				
Fund (1)	12.0%	18.9%	15.5%	15.7%
Market (ASX300)	5.8%	14.6%	8.6%	10.5%
– Excess return	6.2%	4.3%	6.9%	5.2%
– Correlation		-0.13	-0.36	-0.38
Analytics				
Information ratio – OBIF		0.91	0.95	0.79
Tracking error		4.7%	7.2%	6.6%
Sharpe ratio – OBIF		3.4	1.8	1.9
Sharpe ratio – market		1.7	0.6	0.7

Key portfolio changes

Additions/up-weights

Additions

WPL

Up-weights

LYC, SUN, CPU, CBA, WFD, AWC

Deletions/down weights

Deletions

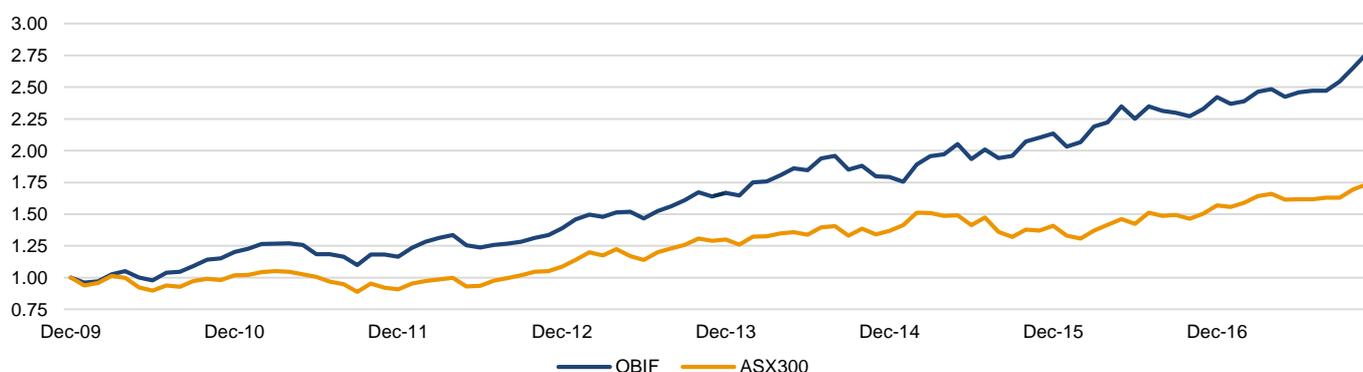
FXJ, VCX, OSH, PLS

Down-weights

ORE

Note (1): Returns from the long portfolio of the ARCO Absolute Trust to Jun16, actual Fund returns thereafter.

Cumulative returns since inception



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