

ARCO Investment Management Benchmark Independent Fund

Monthly report: August 2017

Markets started-down not only a volatile reporting season but also a stronger AUD and escalating geo-political tensions – but for how much longer? The Fund recorded a flat return for the month of August and remains relatively defensively positioned.

August reporting season volatility

Mixed macro-economic signals

Defensive positioning of the Fund

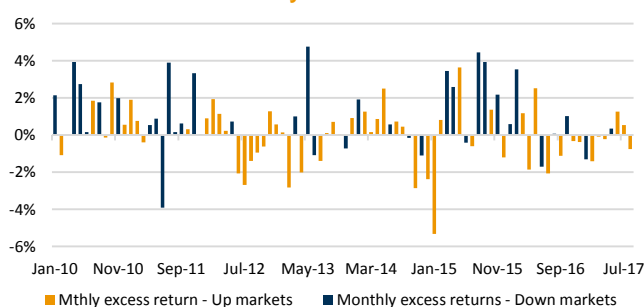
| | Month | Qtr | 1 Year | 3 Year | Life (p.a.) |
|--------------|---------|------|--------|--------|-------------|
| Price NAV | 1.0444 | | | | |
| Fund (a) | (0.01%) | 2.0% | 6.9% | 8.0% | 12.5% |
| ASX300 Accum | 0.75% | 0.9% | 9.8% | 5.0% | 6.7% |

(a) Gross returns from the long portfolio of the Optimal Australia Absolute Trust to Jun 16; actual Fund returns thereafter.

Monthly attribution and top active investments

| Attribution | |
|-------------|---------------------------------------|
| Positive | Banks, energy, diversified financials |
| Negative | Retail, food and staples, transport |
| Top Active | |
| | WOW, CYB, JHG, AHG, ORE, QUB |

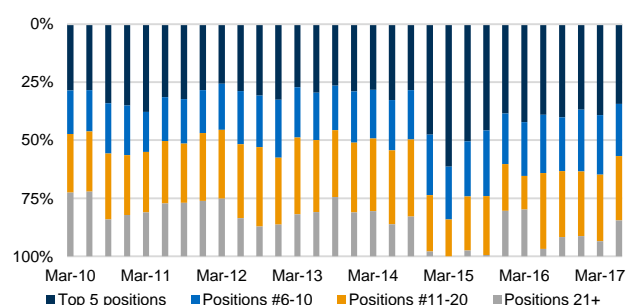
Performance: monthly excess returns



Sector weightings

| | ASX300 | OBIF | Active |
|------------------------|--------|-------|--------|
| Consumer discretionary | 5.2% | 11.1% | 5.9% |
| Consumer staples | 7.1% | 8.5% | 1.4% |
| Energy | 4.1% | 5.6% | 1.5% |
| Financials | 37.4% | 35.1% | -2.3% |
| Healthcare | 6.9% | 0.0% | -6.9% |
| Industrials | 7.2% | 3.9% | -3.3% |
| IT | 1.5% | 6.3% | 4.8% |
| Materials | 16.6% | 16.4% | -0.2% |
| Real Estate | 8.3% | 7.6% | -0.6% |
| Telecommunications | 3.6% | 5.5% | 1.9% |
| Utilities | 0.0% | 2.2% | -2.2% |

Stock concentration - % of equity exposure



Fund strategy and outlook

This fund aims to deliver investors consistent growth over time, with a strong focus on capital preservation and low downside capture.

August was always going to be a relatively volatile month for local stocks as reporting season dominated diaries and financial headlines. Escalating geo-political tensions added further uncertainty. Equity markets have moved into a choppy, sideways grinding pattern as stretched valuations and elevated risks trade off against ultra-low interest rates.

Typifying the tone of reporting season were a number of relatively strong corporate earnings results, with around a third of reporting companies beating their consensus forecast, though a number of them subsequently priced lower on the back of their earnings guidance, capital management pitch or 'surprise' dividend announcement.

Any company's capital management is always going to be in the market's spotlight - not so much what it *has* done, but more importantly what it *plans* to do. Shelving buy-backs (CSL), lifting capex guidance (mining services stocks) and lowering dividend payout ratios (TLS, HVN) will translate quickly into company re-valuation and consequent price action.

Broadly, we remain sceptical about the major banks and healthcare stocks, cautious about the major resource companies and REITs and selectively interested in the consumer discretionary and telecommunications stocks – most especially in stocks that we believe the market punished too harshly for their results and pushed their prices below our fair value range.

As a manager that focuses constantly on preserving investor capital over time, we also remain vigilant of the macro drivers of our equity market. We are of the view that escalating geo-political tensions and a patchy US economic growth story present real risks to investor portfolios at present and need to be taken seriously. As such, the Fund remains relatively defensively positioned with cash readily available to buy into market pull-backs.

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Performance review

The fund traded flat during a relatively volatile month for stock prices amidst the reporting season and we were a little surprised that the broader market continues to shrug-off escalating geo-political tensions.

Of particular note during the month was the strong contribution to investor returns from Orocobre, which we have held for some time. We remain positive on the economics of its existing lithium asset and the potential for treble-gearing its existing equity base over additional production.

Similarly, our long-held positions in CYBG and JHG further rewarded investors in August and are symptomatic of our preference for companies with significant self-help and/or offshore earnings exposure.

CTX and STO were also solid contributors to the fund's return, though our exposure to the insurance (SUN), transport (QUB) and retail (WOW) sectors were detractors for the month.

Through August, we also moved to exit our position in CSL, trim our holding in WOW and take advantage of tactical

opportunities we feel were created during the reporting season to build modest positions in CBA and Telstra which were aggressively sold down.

More broadly, the reporting season delivered its usual mix of frustration, disappointment and delight. Now our attention focuses on reviewing the chorus of capital management strategies proffered during the past few weeks – as always, the devil will be in the detail and delivery – and the market impact of actions on the Korean peninsula plus inaction from the US Congress.

Performance summary

| | Qtr | 1 Yr | 3 Yrs | 5 Yrs |
|--------------------------|------|-------|-------|-------|
| Returns | | | | |
| Fund (1) | 2.0% | 6.9% | 8.0% | 14.3% |
| Market (ASX300) | 0.9% | 9.8% | 5.0% | 10.5% |
| – Excess return | 1.1% | -2.9% | 3.0% | 3.8% |
| – Correlation | | -0.35 | -0.35 | -0.40 |
| Analytics | | | | |
| Information ratio – OBIF | | -0.94 | 0.42 | 0.59 |
| Tracking error | | 3.0% | 7.2% | 6.5% |
| Sharpe ratio – OBIF | | 1.44 | 0.75 | 1.74 |
| Sharpe ratio – market | | 1.09 | 0.24 | 0.61 |

Key portfolio changes

Additions/up-weights

Additions

FXJ

Up-weights

AHG, CBA, CSG, TLS, QUB

Deletions/down weights

Deletions

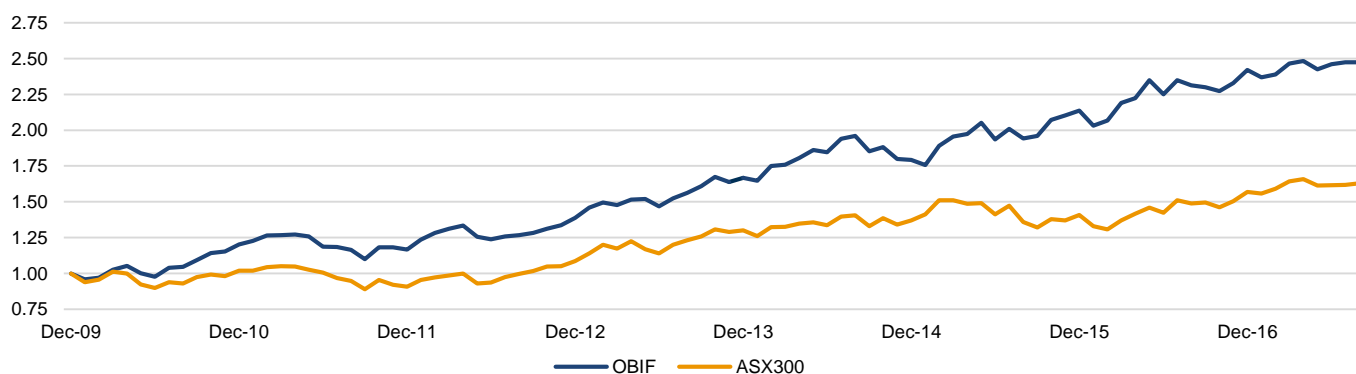
CSL

Down-weights

HVN, SUN, WOW, STO, BHP

Note: Gross returns from the long portfolio of the Optimal Australia Absolute Trust to Jun16, actual Fund returns thereafter.

Cumulative returns since inception



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