Optimal Australia Absolute Trust

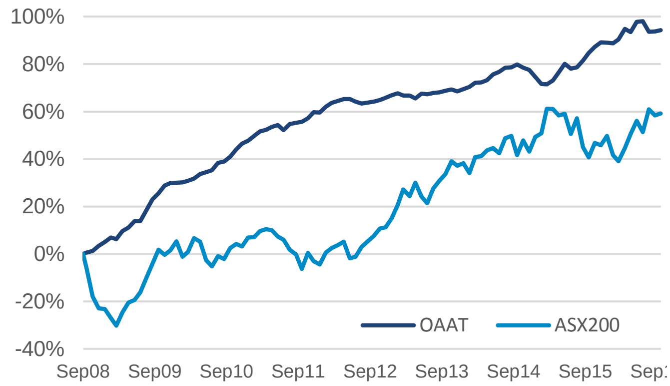
Optimal FUND MANAGEMENT AUSTRALIA

Monthly Report | September 2016

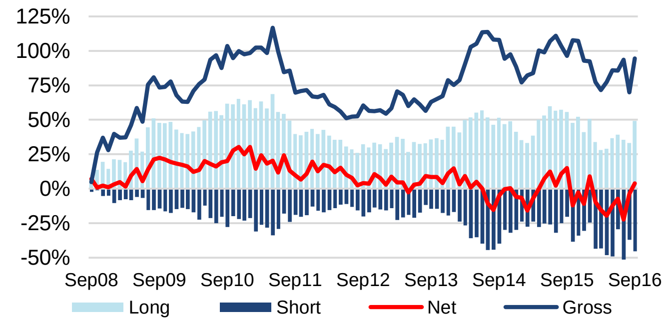
	Month	Qtr	Year	Life (p.a.)
Fund returns	0.6%	-1.7%	5.5%	8.6%
Series 1 NAV				$10.686
Positive months			75%	89%
Worst month			(2.3%)	(2.3%)
Volatility				3.8%
Sharpe ratio				1.2

Monthly key contributors - by sector	
Longs	
Positive	Energy, staples, transport, chemicals
Negative	Banks, resources
Shorts	
Positive	REIT's, transport, media,
Negative	Index futures, non-bank financials

Cumulative performance



Fund investment profile (% NAV)



Risk settings

% of NAV	Long	Short
Equities	49.2%	-23.6%
Debt / Hybrids	0%	0%
Derivatives		-21.8%
Gross exposure		**94.6%**
Net exposure		**3.8%**

Concentration by position	Long	Short
Top 5	23.0%	-17.8%
Top 10	37.7%	-24.2%
Top 15	46.4%	-24.2%

Performance Review

The Trust recorded a net return of +0.6% in September.

In Richard Fisher's memorable words, is the Fed's 'Gordian knot' (1) finally about to finally strangle markets? A harsh recognition seems to be permeating the dense fog within central banks – that this era of monetary experimentation has achieved very little economic growth, but has fundamentally damaged credit creation, among many other unintended consequences.

Markets are highly sensitised to early signals on this theme, as well should they be. Many equity security prices have been grossly inflated by the desperate search for coupon income, and the market has been quick to deal with some of those. But this interest rate repression theme, and vast 'risk-parity' and 'structured product' liquidity flows associated with it have permeated equity pricing in general. Such are the outcomes of severe crowding. A further back-up in bond yields should lead to higher volatility, and could well turn disorderly.

September's equity market featured a continued unwind of the yield trade in the more obvious sectors – REIT's, utilities, and telcos. The Fund had little net exposure here for the month, having flattened out short exposure in these stocks after banking good gains in August.

Materials and resource stocks were strong. We don't think that higher bond yields point to sustainably higher growth and commodity demand, but the Fund did enjoy strong gains in stocks (such as Orica and Aurizon) that have been beaten up by exposure to the commodity complex, and which offered very substantial valuation discounts and/or self-help stories. The Fund's long focus on 'Brexit victims' (Hendersons, Clydesdale Bank) was a substantial drag on performance during the month, but have done much better so far in October.

(1)http://www.dallasfed.org/news/speeches/fisher/2013/fs130805.cfm

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Fund Strategy

Bond yields look to be breaking out, and this is a key signal for stock selection and for the broader direction of equity markets.

So far, signs of a new policy direction are nascent, with talk of 'tapering' QE in Europe, and a shift in Japan to a targeted yield curve. Central Banks will never 'fess up that negative interest rate policies pursued by them with such reckless abandon have severely damaged credit creation, among many other unintended consequences. The dire condition of financial sector profitability in Europe and Japan looks like it has finally crashed its way into the minds of monetary theorists, who prefer to think of policy only in terms of econometric models.

A central irony of the markets is that, eight full years after the Lehman-instigated 2008 crisis, and after unprecedented monetary experimentation, investors are rightly fearful about the solvency of one of the largest (by assets, if no longer by market value) European banks. By what standards are monetary authorities assessing the efficacy of these policies? – certainly not by economic growth and financial stability criteria.

It could still be worse than we think – does the Bank of Japan truly think that a yield curve with a barely measurable positive slope (from -0.10% cash to 0%10-year) is bank profit-enhancing. In the US, which has a more strongly capitalised financial system, the debate within the Fed seems now to whether some tiny "pre-emptive" (really?) action may be the lesser evil relative to more drastic rises after the fact –energy prices can only provide a kicker for indirect (input cost) inflation from here on.

Markets are rightly sensitised to these early signals, as blind adherence to financial repression has been key to the 'Central bank put' so beloved by equity markets in general, and to the extraordinary overweighting of yield in any multi-factor valuation approach. Further, given the massive investment flows into equity markets of structured yield or 'risk-parity' products (which typically use leverage to juice-up coupon returns), any bond yield-based unwind has the potential to turn disorderly. There are good reasons to maintain a defensive posture towards market risk.

Optimal Australia Absolute Trust – monthly returns

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FY
FY17	(2.28%)	0.02%	0.56%										(1.68%)
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%	11.2%
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 15/9/08

Optimal Australia Absolute Trust – distribution history

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

Fund facts

Initial series NAV	$10.686	**Distribution frequency**	Yearly (bi-yearly in FY 2016)
Strategy	Long-short Australian equities	**Minimum investment**	Wholesale investors only, $100k
Objective	Positive returns in all market conditions. Overarching focus on capital protection	**APIR Code**	OPT0001AU
		ISIN	AU60OPT0014
Firm AUM	$100m	**Bloomberg**	OPAUSAB AU Equity
Last distribution	$0.265 per unit (July 2016)	**Fund inception**	15/9/08 at $10.000 per unit