

ARCO Investment Management Benchmark Independent Fund

Monthly report: July 2017

Currency headwinds impacted the market and our fund in July. The Benchmark Independent Fund realised positive alpha performance during the month and we remain mindful of broadly expensive stock prices and the usual trials of the company reporting season.

July: positive alpha return month

Stock valuations remain demanding

Cash available for price pull back

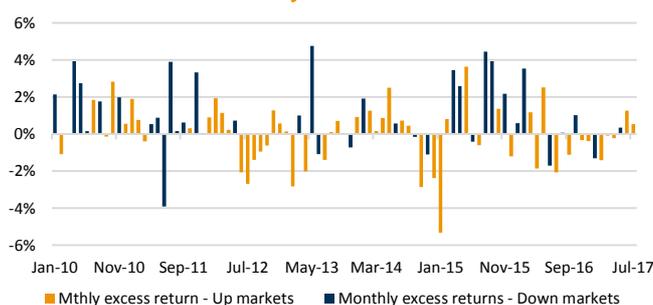
	Month	Qtr	1 Year	3 Year	Life (p.a.)
Price NAV (ex-dist)	1.0444				
Fund (a)	0.54%	(0.4%)	5.3%	8.4%	12.7%
ASX300 Accumm	0.01%	(2.6%)	7.3%	5.0%	6.7%

(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	Retail, Energy, Healthcare
Negative	Resources, Banks, NBFIs
Top Active	
	WOW, CYB, HT1, HVN, CTX, CSL

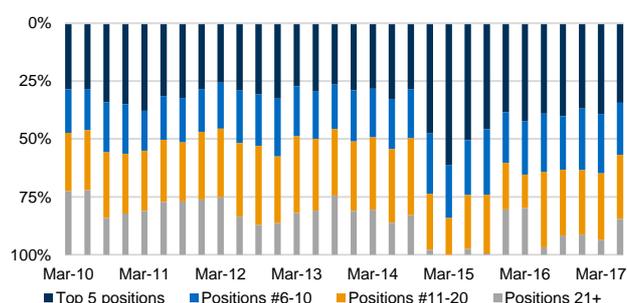
Performance: monthly excess returns



Sector weightings

	ASX300	OBIF	Active
Consumer discretionary	5.2%	9.2%	4.0%
Consumer staples	7.1%	9.9%	2.8%
Energy	4.1%	7.4%	3.3%
Financials	36.9%	34.1%	-2.8%
Healthcare	7.5%	4.5%	-3.0%
Industrials	7.4%	2.9%	-4.5%
IT	1.5%	5.8%	4.3%
Materials	16.0%	16.3%	0.3%
Real Estate	8.3%	5.5%	-2.8%
Telecommunications	3.8%	4.4%	0.6%
Utilities	2.3%	0.0%	-2.3%

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.

July was not an easy month for the Fund. Pleasingly, our stock selection delivered a positive return to investors. The AUD strengthening made its mark though. Our focus for some time has been on structural and cost-out drivers of earnings growth, with a broad aversion to facing the Australian consumer. As a result, the portfolio is materially exposed to non-AUD earnings and asset values, and suffered from the strong rise in the AUD. The currency also hit the broader market, which was weighed down by the pervasive influence of (unhedged) "carry" investors, who were (and probably are still) selling to lock-in very strong returns in USD terms.

Our thinking on markets and risk has not changed greatly. GMO's James Montier sums it up pretty well:

"My perspective is that we have a bubble of complacency, and people are acting as if there are no risks, while I see a world full of them... And yet pretty much all assets look to be priced for perfection..."

July saw central banks execute any number of 10-point degree of difficulty linguistic contortions around the "neutral rate" debate, and in trying to reassure investors that they don't really mean what they say when earlier floating the possibility of withdrawing monetary stimulus.

So it was in Australia with the RBA, no doubt horrified by the economic impact of a rampant AUD, urging that "no significance" should be read into the discussion of a "neutral nominal cash rates of 3.5%" in its July minutes. Better hope so – consumer mortgage stress is evident (albeit so far in only certain demographic pockets) despite interest rates at generational lows, and the general consumer slow-down in the June quarter highlighted this broader sensitivity to interest rates.

ARCO Investment Management Benchmark Independent Fund

Monthly report: July 2017

Performance review

As noted, July's performance was solid in view of the headwinds represented by the much stronger AUD on the Fund's weighting to offshore earnings. While generally not fans of the Australian consumer economy, we have been invested in several retail stocks, as we consider their discount to our fair value assessment to be simply too great, with stock prices so heavily influenced by short selling and the fear that no local retail business model can survive Amazon's imminent arrival. In July, Harvey Norman, Woolworths, and Auto Group were among our better performers, and we continue to believe there to be considerably more to the

investment case than a valuation discount.

The Fund's commodity and energy exposure, while small, also generated positive returns, with strong stock price gains from Santos, BHP, and our smaller positions in the emerging lithium producers.

Our active underweight positions in financials were negatively impacted by the slight retracement in the yield curve, and also by the market's interpretation that APRA's 'unquestionably strong' capital buffers for the Australian banks (CET1 ratios of at least 10.5% by Jan-

2020) implied lower than expected capital shortfalls.

We are now immersed in the August company reporting period: "the moment of truth" for many stocks. It is early days, and the market has been typically unforgiving of any earnings or guidance miss, such as for Crown Resorts or James Hardie. So far, the Fund has only had one earnings report for a larger portfolio holding, for CYBG, which the bank passed with flying colours. The full earnings season is unlikely to be so easy.

Performance summary

	Month	Qtr	1 Yr	3 Yrs	5 Yrs
Returns					
Fund (1)	0.54%		5.3%	8.4%	14.5%
Market (ASX300)	0.01%		7.3%	5.0%	10.8%
- Excess return	0.53%		-2.0%	3.4%	3.7%
- Correlation			-0.37	-0.35	-0.40
Analytics					
Information ratio – OBIF			-0.67	0.48	0.56
Tracking error			3.0%	7.2%	6.5%
Sharp ratio – OBIF			0.95	0.80	1.76
Sharp ratio – market			0.73	0.20	0.64

Key portfolio changes

Additions/up-weights

Additions

Nil

Up-weights

WOW, HVN, BHP, LNK, ANZ

Deletions/down weights

Deletions

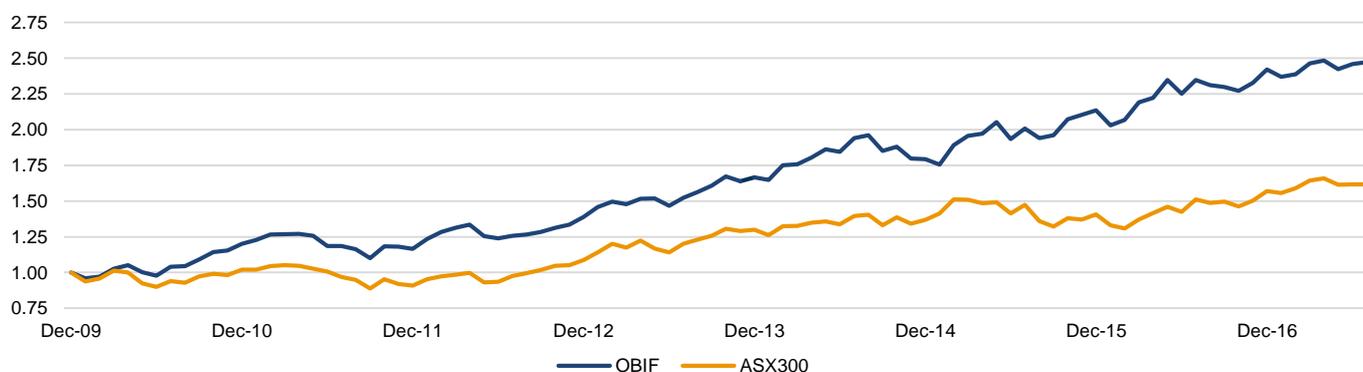
HT1, WES

Down-weights

CSL, CYB, GXY, ORE

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

Cumulative returns since inception



ARCO Investment Management Pty Ltd
ABN 48 129 937 837 AFSL 325 159

Level 2, 121 Flinders Lane
Melbourne VIC Australia 3000

T +61 (3) 9660 9500
F +61 (3) 9660 9599

E info@arcoim.com
arcoim.com

This report is prepared for investors in the Optimal Benchmark Independent Fund. Returns and prices are quoted net of all expenses, management fees, and accrued performance fees unless specified otherwise. This is neither an offer to sell nor a solicitation of any offer to buy Units in the Trust. Any such offering can only be made to qualifying 'wholesale investors' pursuant to the Fund's deed, and the relevant subscription application.