Atlantic Pacific Australian Equity Fund

ARSN 158 861 155

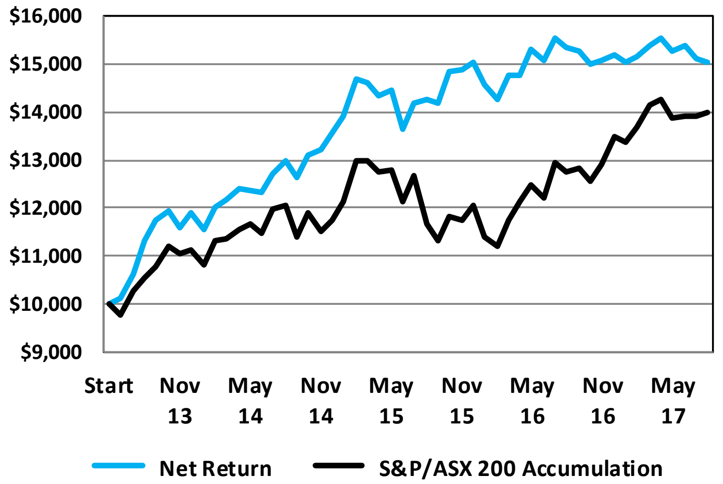
Fund Monthly August 2017

Return Summary

Period	1 mth	3 mth	6 mth	1 yr	3 yr (pa)	Cumulative	Per Annum
Fund Return	-0.8%	-1.6%	-1.0%	-2.2%	4.9%	50.2%	10.0%
S&P/ASX200 Acc.	0.7%	0.9%	2.4%	9.8%	5.1%	40.0%	8.2%
Excess return	-1.5%	-2.5%	-3.4%	-12.0%	-0.2%	10.1%	1.8%

Fund Returns are prepared on a redemption unit price basis after management and performance fees inclusive of GST. Distributions are assumed to be re-invested at the mid unit price. Individual tax is not taken into account in deriving Fund Returns. In calculating the NTA, the Atlantic Pacific Australian Equity Fund ("Fund") asset values have been calculated using unaudited price and income estimates for the month being reported. Past performance is not indicative of future performance.

Cumulative Returns of $10,000



Fund Strategy

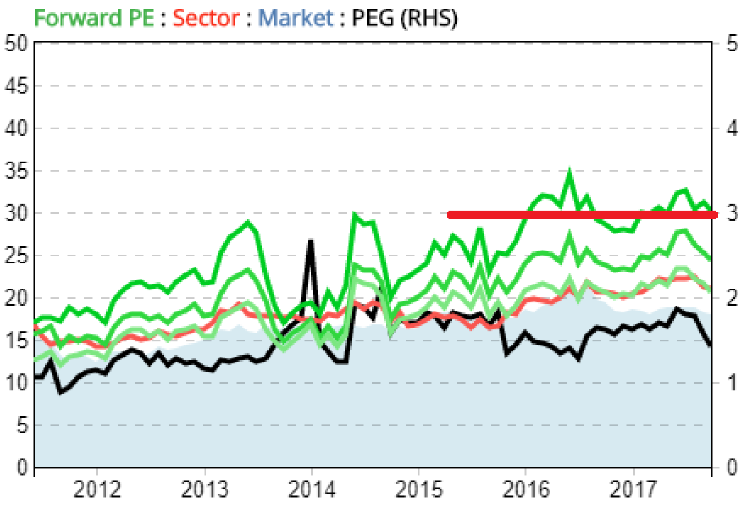
The Fund is a long-bias equity market product which typically buys or short sells Australian listed securities and derivatives. Net and Gross market exposure is maintained within a range of 0-100% and 0-200%, respectively.

The Investment manager employs their Quadruple Alpha Investment Strategy which focuses on outperforming over all market cycles by capturing upside returns while minimising downside risk.

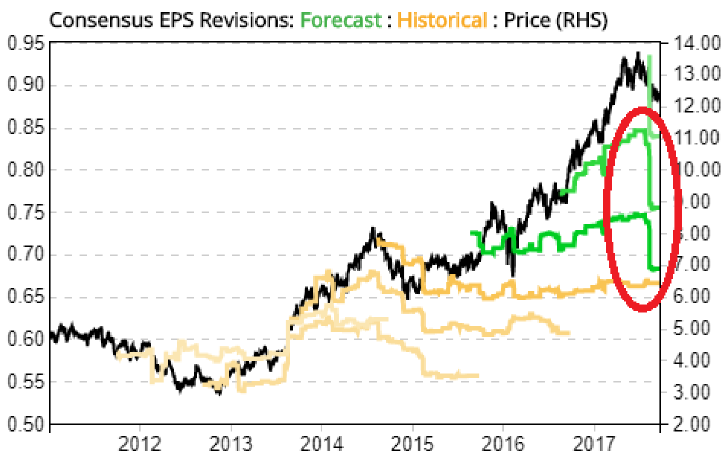
The objective of the Fund is to outperform the benchmark by greater than 5% pa after fees over a 5-7 year time frame.

Market Overview

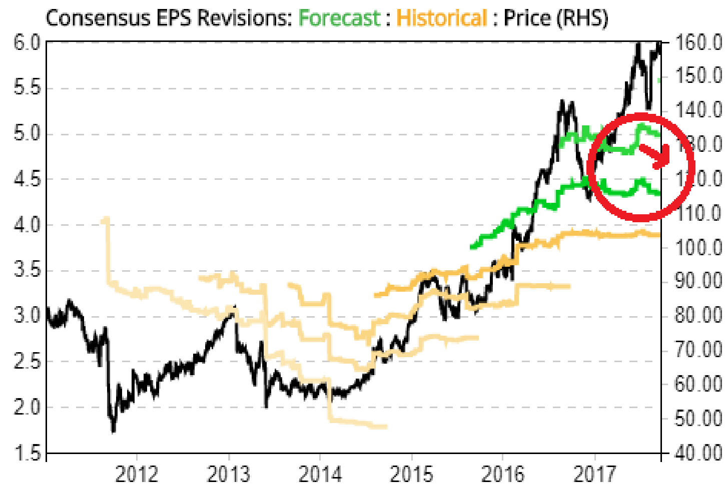
- The Australian equity market rose 0.71% in what was a lack-lustre reporting period for most companies. On review of company reports, there were few major surprises or change in earnings other than the typical handful. Commonwealth Bank (CBA) reported ahead of expectations assisted by all-time low provisions. It's remarkable to see earnings per share (EPS) projections now above post "bank tax" downgraded levels driven solely by a lack of provisions. BlueScope Steel (BSL), after having been ramped almost 90% since November 2016, was a clear underperformer over August 2017. The Fund had not participated in this rise over the year but had taken short positions from time to time. This company has been quite difficult to take a position in either way (long or short) and while we made money on the short position during July 2017 after having been in an overbought state for an extended period of time, we had covered prior to their result...the one that got away! Insurance Australia (IAG) presented as a peculiar outcome where prior to their official report they upgraded their earnings. However, when they reported, the quality of the result was very poor. At times, we see companies attempt to game the reporting season but the market sees through these grandiose plans. Vocus Group (VOC) performed very poorly over the month with a reversion in price of over 30%. This was in part due to takeover talks stalling and their reporting of very large write-downs. The write-downs were associated with acquisitions the M2 Group undertook in prior years (M2 Group [Prior ASX Code: MTU] was consolidated into VOC via an effective reverse takeover) driven by reductions in expected earnings over forecast years as well as massive increases in the discount rate used to value these companies. All-in-all, a sobering outcome showing how the initial euphoria of over-zealous management expectations around the time of the prior acquisitions have impaired significant capital in the company. The Fund has not been involved in this company recently given the binary outcome of takeover scenarios and the weak state of the telecommunications industry.



Treasury Wine Estates (TWE), a company we had liquidated in prior months due to valuation concerns (see valuation chart to right at all-time highs) and opaque earnings trajectory in our view, was the star performer over reporting season rising almost 20%. On review of their report and subsequent market analyst revisions, there was very little change in their earnings and continue to question how the company's shares can trade so highly. And while there should be some rejoice from the activation of a buy-back of circa 3% of total outstanding shares, we find these actions by management distorting as cashflow conversion has dramatically reduced. Either way, its remains too expensive for the time being. The Fund had exposure to Orora Limited (ORA) through the reporting season. The company (since spinning off from Amcor (AMC)) has been able to sustain a stable earnings profile with quite low earnings variability. The company had been sold-off to the bottom of its recent trading range prior to their report for no particular reason and so we took the opportunity to top up the Fund's position. And while there was again very little change in earnings expectations post report the company's shares have firmed since. Challenger Limited (CGF), a company we have had involvement since the inception of the Fund surprised us the most. The company has been owned for many reasons (exposure to the ageing demographic driving structural demand for annuity products and rising equity markets) but more recently the very large move into the Japan annuity space (the Japanese annuity market being many multiples of the size of the Australian market!) remains an exciting venture moving forward for the company. However, we were not expecting an "at-market" strategic capital raising of circa 6% of capital to MS&AD (A Japanese insurer) which has been taken negatively somewhat. The operating performance of CGF was slightly better than expected but with the extra capital led to 5% downgrades to earnings per share over the forecast horizon (see chart to below showing CGF EPS revisions over time). And while to see the price re-trace over 10% in the short term, in our view this is a small price to pay for what will be a deal that will support their earnings growth potential over years to come.



Added to this is the intention of MS&AD to raise their stake in CGF to 10% via on-market purchases. The Fund was also hit by a capital raising in Mesoblast (MSB). This company is renowned for having poor performance during capital raisings as it seems to be a favourite of the short sellers. Any hint of a capital raising leads many of these Fund Managers with the instinct to sell. The company stopped trading into a small rights issue around $1.60. The theoretical ex-rights price was determined to be $1.59 with a rights price of $1.40. The company ended trading for the month at a massaged $1.44. To have this deeply discounted capital raising placed in front of you at the end of the month is very frustrating to say the least given the potential of the company over the coming years. Another detractor over the month was in the short position the Fund had in Qantas (QAN). We had entered this position post a double overbought state (very rare and usually rewarding). Over July the price reverted positively in our favour but over the ensuing month of August 2017, the share price rallied into the result. Once again, nothing amazing had been reported by QAN but the price has stood its ground. The Fund re-entered into a position in Nanosonics (NAN) during the month after selling out in June 2017 (tax loss related selling). Nanosonics has had an awful price trajectory over recent times which has been brought about by a change in business model in new markets. Effectively the company has moved into a heavier capital model which dampens earnings now but improves payoffs into the future…it would appear investors have discounted this model. We re-entered the company's shares around $2.23 not too far away from the recent low point following the announcement by the company that they had improved their contract with GE Healthcare in the US, one of their largest distributors. While the impact of this contract is quite some years away, the certainty this contract revision now provides has improved sentiment towards the stock. Nanosonics will remain a core holding for the foreseeable future. Another exposure that performed well over the month was Cochlear (COH). To us the performance was merely a reversion from the prior month which fell 8% and then retraced 9% during August 2017 post their report. It is mind boggling to us some of the price moves that occur because in Cochlear's case, earnings were downgraded (see chart to right showing Cochlear EPS revisions over time)! We were a little worried of the result after first glancing the downgrades to the out years but then to see the price bounce so hard and so quickly just leaves us with the impression that not everything that goes on in markets can be explained logically!



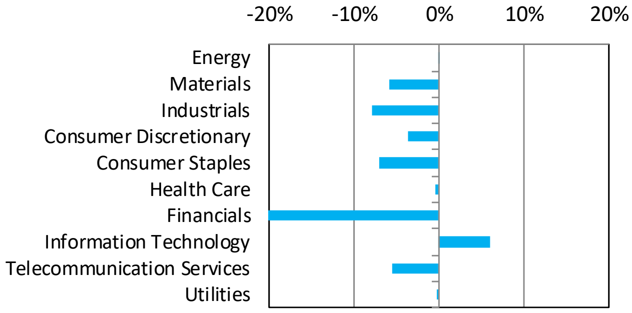
Apart from the above Fund activity, we have been busy beavering away on the next iteration of the PDS. We don't often mention but we believe it is in your interests to understand that we are always moving forward with regulatory changes. These regulatory changes are designed to further protect your interests and we welcome change if protections for unitholders are improved. The current program of work has focussed on the new Fee disclosures for every Managed Investment Scheme in Australia (ASIC – Regulatory Guide 97), a new taxation Scheme for Managed Investment Schemes called AMIT (Attribution Managed Investment Trust) and greater protections against identity theft for unitholders and stronger requirements on our part relating to unitholder privacy. While all are big picture issues, they are fundamental to the future of the industry. If any unitholder has any query on the specific changes that have been put in place, please email us and we will be happy to provide further detail.

Outlook – As was noted last time we wrote, the trading range of the Australian market has been peculiar and this range has now persisted for another couple of months while other markets have generally traversed positively. We find this perplexing as on the one hand the market rallies with overnight markets and positive local economic data but is then sold back down. Some other rally occurs on very little news to take the market back up to the top of the trading range again. We don't quite understand why this is occurring and today are no closer to finding out why the Australian market has failed and recovered 4 times. While there are certainly plenty of conspiracy theories out there (Global investors selling our market down to invest in other markets say), we can't be certain this is the case as there remains plenty of cash on the sidelines. It is also remarkable that our market tends to react negatively to geo-political issues more so than other markets on any day. So, while the economic trajectory has been stable in Australia supported by infrastructure projects and a generally buoyant eastern-side economy, we have yet to see this translate to equities this year. We are generally prepared for rising markets but need to offset this against geo-political issues that are taking hold now. The market implications from the North Korean Crisis we don't believe has been correctly priced-in across the world. In our view, the level of euphoria in equity markets globally is not pricing a negative event whether of North Korean initiation or not. Similarly, a forced slowdown in China has not been priced which is now taking hold. On a more positive note which relates to the large Australian banks. We had thought the ability for the banks to reach "unquestionably strong" capital levels in time to ward of rising provisions against Australian house prices was unlikely but with recent asset sales and further asset sales in the pipeline, they should be able to attain the necessary capital levels comfortably.

Risk Statistics

	Fund		Index	
	3 Year	Inception	3 Year	Inception
Alpha (%pa)	-0.2%	1.8%		
Downside Capture	58%	61%		
Standard Deviation	8.3%	8.8%	12.2%	11.5%
Sharp ratio	0.9	0.1	0.6	0.1
Sortino		1.4		1.4
Largest Drawdown	-7.1%	-7.1%	-13.7%	-13.7%

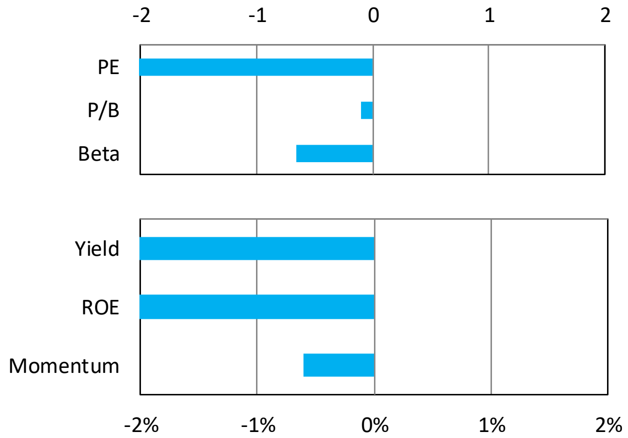
Sector Exposure



Exposure

	Long	Short	Net	Gross
Equity	52%	-4%	48%	56%
Index Futures			0%	0%
Net	52%	-4%	48%	56%
Cash			52%	

Factor Exposure



Contribution

Positive	Negative
Amcor	Commonwealth Bank
Nanosonics	Mesoblast
Orora	Qantas
Norward Systems	Universal Coal

Fund Information

APIR Code	OMF0003AU	Responsible Entity	Equity Trustees Limited
Inception	1 June 2013	Investment Manager	APSEC Funds Management
Minimum Investment	$10,000	Administrator	FundBPO
Application/Redemption	Monthly	Custodian	FundBPO
Management Fee	2.0%	Prime Broker	Interactive Brokers LLC
Benchmark	S&P/ASX200 Accumulation	Auditor	PriceWaterhouseCoopers
Performance Fee	15% above S&P/ASX 200 Accumulation + 3%pa subject to a high water mark		
AUM of Fund	AUD$26.19m	Application Price	1.2938
Mid Unit Price	1.2925	Redemption Price	1.2912

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Important information

APSEC
FUNDS MANAGEMENT