Atlantic Pacific Australian Equity Fund

ARSN 158 861 155

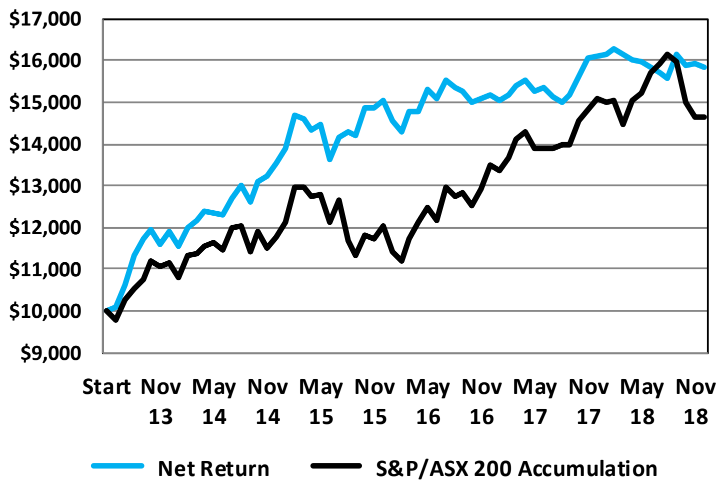
Fund Monthly December 2018

Return Summary (To December 2018)

Period	1 mth	3 mth	6 mth	1 yr	3 yr (pa)	5 yr (pa)	Cumulative	Per Annum
Fund Return	-0.64%	-1.7%	0.1%	-1.5%	1.8%	6.2%	58.5%	8.5%
S&P/ASX200 Acc.	-0.12%	-8.2%	-6.8%	-2.8%	6.7%	4.3%	46.4%	7.0%
Excess return	-0.52%	6.5%	6.9%	1.4%	-4.9%	2.0%	12.1%	1.5%

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.

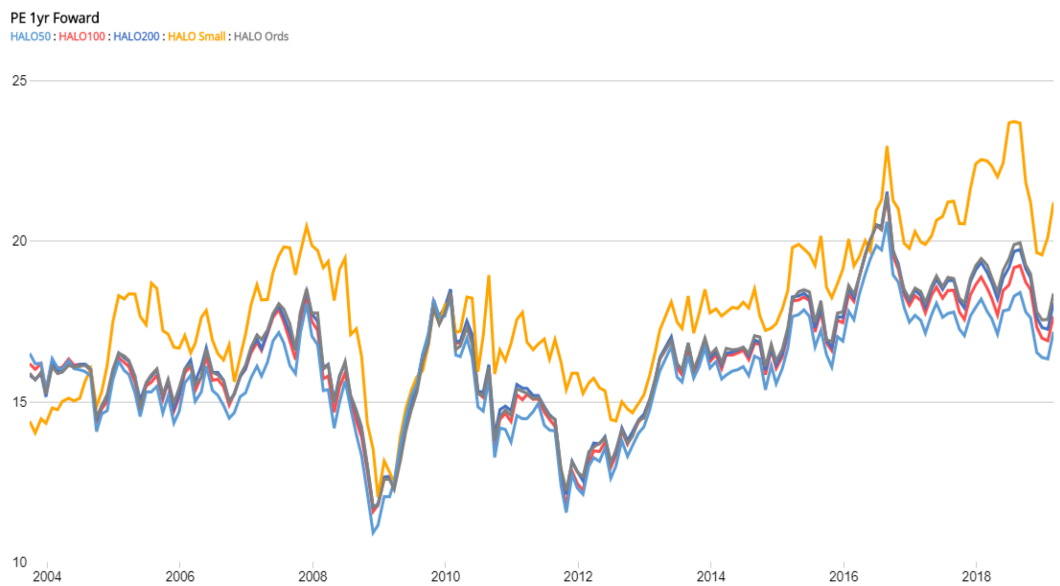
The Investment manager employs its Quadruple Alpha Investment Strategy which focuses on outperforming over all market cycles by capturing upside returns while minimising downside risk.

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

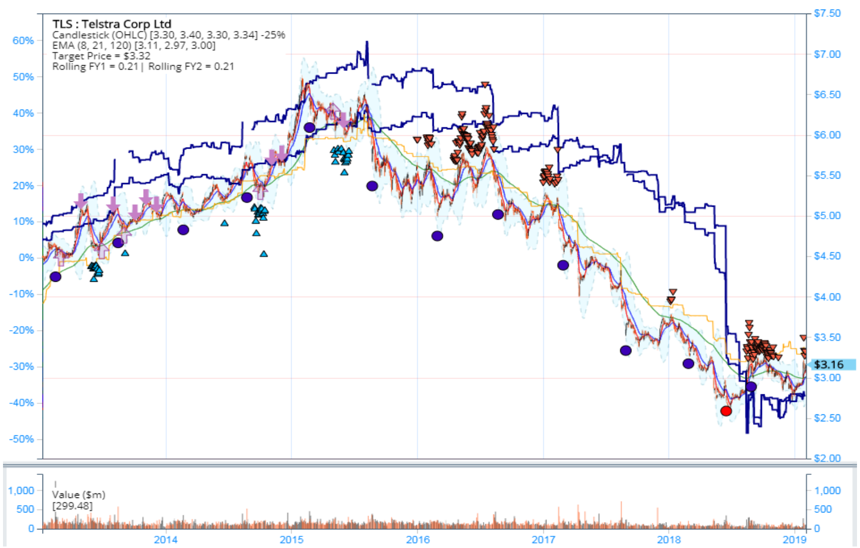
The Australian equity market continued to track downwards slightly through December 2018, finishing the month with a slightly negative return of -0.12%. This was the worst December recorded by our market since 2011, and no doubt surprised many, who perpetually seem to expect the Santa rally regardless of overarching market concerns.

Post hitting intra year highs in Q3, the Australian market shed 11%, to finish the CY18 period in negative territory. The index returned -2.8% for CY 18, with 4.1% of that coming in the form of dividends. This poor performance came as no great surprise to us, being that we have been alert to the drivers of these falls for some time now. The surprising element, in our view, was the extended period of time that it took for glaring macro risks to show themselves in the price performance of our market. With the market now having retraced significantly from its peak no doubt you will be hearing many calls that the broader market is now a ‘buy’ based upon valuation alone. In our view this provides an incomplete and erroneous explanation, while valuations are certainly looking more reasonable, they remain elevated by historical standards, and regardless, they are not the determinant of share price performance anyway.



The index constituents displayed a wide divergence of sectoral returns for the month of December 2018, with the Materials sector being the standout performer adding over 5% throughout the month. This was driven by a resurgent Iron Ore price which added over 10% throughout the month supporting surges in BHP and RIO of 11.5% and 7.1% respectively. Similarly, FMG has performed remarkably, and at the time of writing is sitting up 65% higher than its 2018 lows. In December crude oil prices continued their 2018 retracement, falling a further 11% to USD$45 per barrel. Although, in their case at least perhaps Santa really did arrive, with the 25th December marking the start of a bounce in crude futures from USD$43 to their current level of nearly USD$55. While we anticipate seeing periods of strong performance in various activity linked commodities, such as the bounce in Iron Ore prices and crude, in our view these do not represent turning points in the absence of supportive underlying activity data. With Chinese Manufacturing PMI's continuing to print negative (sub-50) numbers, and the December trade balance showing a contraction in trade, it is hard for this back drop to support a sustained positive delta.

Financials had a poor month, falling 3.1% throughout December, being led lower by the major banks which were generally weaker throughout the month (although not entirely, see Commonwealth Bank of Australia – CBA:ASX). This capped a year of horrible performance for Australian Financials, with prices falling by nearly 18% for CY 18, and a total return (including dividends) of -9.7%, which is hardly surprising given the stage in the housing market cycle we are currently in. The worst performing sector of the month of December, and CY2018, was Communication Services, which fell 5.1% for the month and recorded a return of -21.4% for the year. This was against a backdrop of increased competition as a result of the NBN, and a much more challenging competitive environment moving forward. The fall from grace for a number of these telco names has been spectacular, and we have no doubt that many investors have held them throughout the entirety of the down move, perhaps the most likely candidate for such behaviour is former dividend-darling Telstra (TLS:ASX), which has managed to erode a lifetimes worth of dividends in the form of capital loss in the last 3 years. In our view there was ample warning, and a quick scan of HALO provides evidence of numerous exit points and/or opportunities to go short.



Fund Activity

The month of December saw us enter the month in a state of continued heightened risk mitigation, expressed via a number of short positions, and greatly reduced market exposure. As a result, our SPI Futures hedging strategy was the main positive contributor to fund performance throughout the month with active management of the funds' beta exposure adding value both in the early and final third of the month. Ultimately the rally at the back end of the month, from the 27th December onwards, resulted in us giving back a significant portion of the profits derived from the hedge, which we closed on the 28th as a result. This active management of beta exposure has been very rewarding for fund investors since the inception of the fund, and while we will never be able to perfectly time entries and exits, it has been shown to add significant value over time.

The second largest contributor to fund performance this month was Universal Coal (UNV:ASX), which we have written about a number of times in the past. The stock climbed steadily throughout the month and hit an intra-month high of 35c. We trimmed the position at various points in time throughout the month, at prices that we considered good enough to sell into.

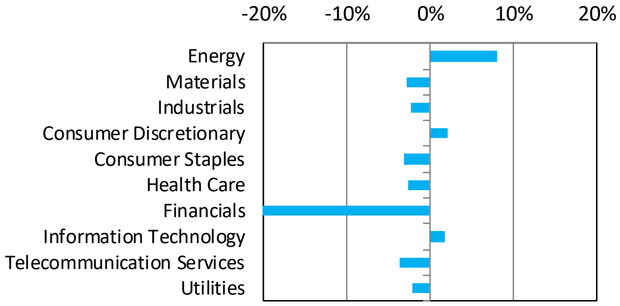
Another positive contributor, CSL Limited (CSL:ASX) added 0.15% to fund performance throughout the month and is a perfect example of the powerful signals generated by the HALO platform which we use as an integral part of our process. In this case the much-lauded 'Fakey-Shakey' came to the fore, which identifies companies experiencing a divergence between their EPS revisions and share price performance. Looking at the chart of CSL below clearly shows that the 'Fakey-Shakey' signal (being the blue upward pointing arrow) was triggered multiple times throughout September, October, and December, providing accumulation points for patient investors.

Detractors from fund performance for the month included WPL, which we bought on the 3rd December having seen the price of the underlying (i.e. the oil price) and the stock both stabilise and appear to reach support. The oil price fell sharply from its October peak, and appeared to rebase and stabilise in late November. The sheer size of the move (Oil Futures fell from a high of USD$78, to a rebased level of approximately USD$51) suggested to us that the asymmetry was to the upside, with a period of consolidation from late November to mid-December forming the rebased level with upside to come. Buying WPL in early December we exited the trade at a loss when the oil price took a leg lower on the 18th December. Ultimately the oil price did bounce, and brought the Oil sector including WPL with it, but not before touching USD$10 below where we thought it had rebased. Ultimately, being willing to liquidate positions that aren't working quickly is part of the risk management process of the Fund and is one of the reasons that we have avoided the downdrafts in performance that plague other managers.

Risk Statistics (As at December 2018)

	Fund		Index	
	5 Year	Inception	5 Year	Inception
Alpha (%pa)	2.0%	1.5%		
Downside Capture	46%	47%		
Standard Deviation	5.9%	8.1%	9.8%	10.9%
Sharpe ratio	0.6	0.8	0.4	0.5
Sortino		1.4		1.1
Largest Drawdown	0.0%	0.0%	0.0%	0.0%

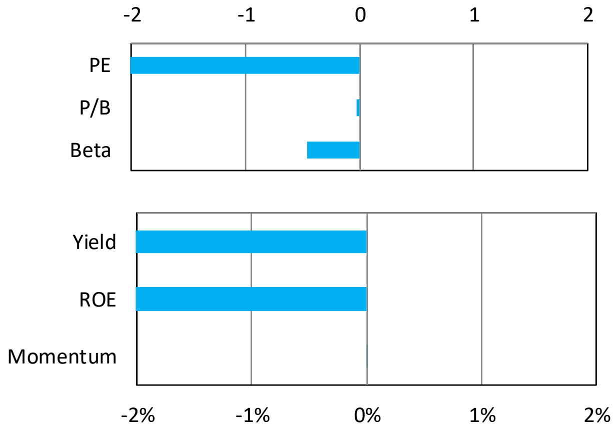
Sector Exposure



Exposure

	Long	Short	Net	Gross
Equity	70%	-8%	62%	78%
Index Futures	0%	0%	0%	0%
Net	70%	-8%	62%	78%
Cash			38%	

Factor Exposure

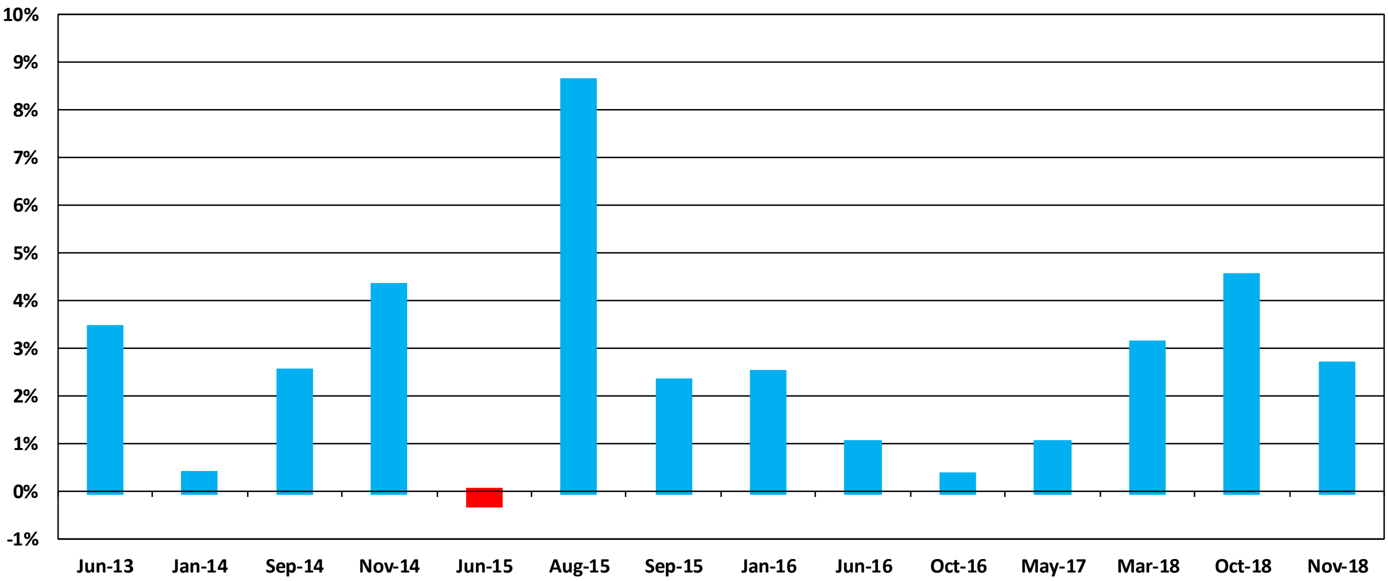


Source: APSEC Funds Management

Contribution

Positive	Negative
CSL (Long)	Brookside Energy (Long)
Fortescue Metals (Long)	Corporate Travel (Long)
IOOF Holdings (Long)	The GO2 People (Long)
Universal Coal (Long)	Woodside Petroleum (Long)

APAEF Relative Returns (From Inception)
When the market is down more than -2%



Source: APSEC Funds Management

APSEC FUNDS MANAGEMENT

Fund Information (As at December 2018)

APIR Code	OMF0003AU	Responsible Entity	Equity Trustees Limited
Inception	1 June 2013	Investment Manager	APSEC Funds Management
Minimum Investment	$10,000	Administrator	Mainstream Group Holdings Ltd
Application/Redemption	Monthly	Custodian	Mainstream Group Holdings Ltd
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		
Mid Unit Price (ex Dist)	1.2361	Application Price (ex Dist)	1.2373
		Redemption Price (ex Dist)	1.2349

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Important information