Optimal Australia Absolute Trust

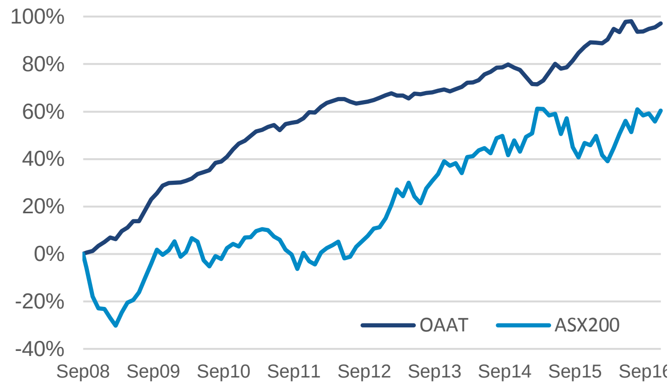
Optimal FUND MANAGEMENT AUSTRALIA

Monthly Report | November 2016

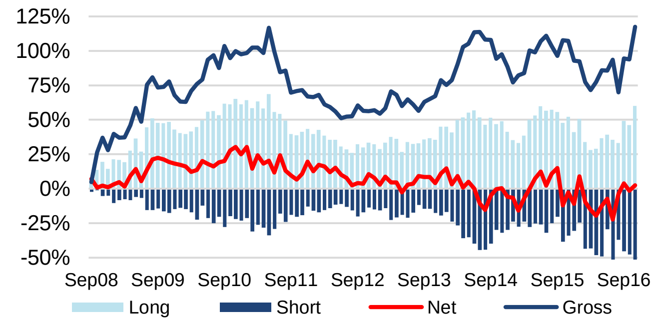
	Month	Qtr	Year	Life (p.a.)
Fund returns	1.0%	1.9%	4.3%	8.6%
Series 1 NAV				$10.825
Positive months			75%	91%
Worst month			(2.3%)	(2.3%)
Volatility				3.8%
Sharpe ratio				1.24

Monthly key contributors - by sector	
Longs	
Positive	Resources, media, banks, retail
Negative	Telecoms, staples
Shorts	
Positive	REIT's, infrastructure, media
Negative	Resources, diversified financials, index futures

Cumulative performance



Fund investment profile (% NAV)



Risk settings

% of NAV	Long	Short
Equities	60.0%	-31.3%
Debt / Hybrids	0%	0%
Derivatives		-26.3%
Gross exposure		**117.5%**
Net exposure		**2.4%**

Concentration by position	Long	Short
Top 5	21.4%	-18.6%
Top 10	38.3%	-27.1%
Top 15	51.5%	-30.8%

Performance Review

The Trust recorded a net return of +1.0% (Series 1 units) in November.

The Australian equity market enjoyed a decent rebound in November, fuelled in large part by a surprisingly quick embrace of Trump 'reflation' – an essentially bullish view on the impact of fiscal stimulus and corporate tax cuts under the new US administration. This trade was expressed through a sharp rotation out of high-yield and defensive sectors into cyclicals, especially resources, which were super-charged by a rampant commodity complex centred on the Dalian futures exchange. Financials also performed strongly in many markets, with a steepening yield curve and perceptions of regulatory roll-back, for example of Basle IV capital requirements locally, and pretty much everything in the US under a laissez-faire Trump Presidency.

This is the easy part. At this point in the political cycle, policy formation (much less execution) runs a distant second to imagination. Driven in part by significant crowding and extreme investor positioning, markets can continue to run with a theme until facts get in the way. The one fact that could well unsettle markets is the new reality of higher bond yields, and structurally higher inflation. Financial repression as practised by central banks (and the vast 'risk-parity' and 'structured product' liquidity flows associated with it), have had a fundamentally distortive effect on equity pricing in general, and that game appears very nearly over.

The Fund's stronger performers included our holdings in financials (ANZ, Clydesdale, Suncorp, Hendersons), resources (Orocobre) and materials. The Fund initiated a new long position in APN, which has rationalised itself down to two attractive media exposures in radio and outdoor advertising, and at a discounted valuation arising from technical pressure around its recent capital raising. Hedging market risk through short selling was successful in interest-rate sensitive stocks, and very difficult elsewhere.

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Fund Strategy

The Fund's key objective is to compound investor returns by focussing on stock alpha. The Fund had slightly positive net market exposure (+2.4% of NAV) at month-end, and retains some scepticism about the sustainability of the 'Trump bump'. Our thinking is:

- The market narrative is for a growth breakout, yet the US business cycle is already extended by historical standards. In the words of Jeffrey Gundlach (who now seems equally prescient on US politics as on the bond market): *"The bar was so low on Trump… now this guy is the Wizard of Oz and expectations are very high. But there's no magic here..."*
- It is difficult to understand whether the massive increase in bulk commodity prices over the last quarter reflects a sustainable increase in Chinese steel demand, or (as Barclay's John Clemmow contends) a third attempt to bail-out China's heavily-indebted basic industry SOE's, this time via the commodity markets.
- Either way, beware the bonds. Higher deficit spending in the US and commodity price rises should impact perceptions of future inflation. OPEC's efforts to push oil prices up should add fuel to this fire. Bond yields in the US and Australia seem very likely to track higher.
- We've been surprised by how little sensitivity broad equity indices have shown to higher bond yields – leaving aside the bloodbath in defensives and REIT's. This theme remains a very big deal. Financial repression has been key to the 'central bank put' so beloved by equity markets, and to the overweighting of yield.
- It's possible that market distortions resulting from the vast liquidity creation by central banks over recent years can unwind smoothly, but dislocation seems equally possible.
- Market technical are not universally positive. Liquidity in the high-yield bond market continues to deteriorate. Locally, the IPO market was showing clear indigestion, with even re-priced deals struggling (e.g. Inghams, Bravura). A number of market darlings have missed earnings, with horrific price reactions (Isentia: -27%,Vocus: -25%, Bellamys -44%) and the small/mid cap market has fallen sharply.

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%	0.35%	0.95%								(0.40%)
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%	11.21%
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	$10.825	**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