

# ARCO Investment Management Absolute Trust (Optimal Australia Absolute Trust)

Monthly report: September 2017

Despite escalating geo-political tensions and global interest rate risks, plus more signs of a peak in domestic housing, market volatility nears record lows – is this sustainable? The Absolute Trust recorded a strong return for the month of September and remains defensively positioned.

Performance	Month	Qtr	1 Year	3Yr(pa)	Life (pa)
Fund return (net)	2.79%	2.73%	5.45%	4.54%	8.28%
Positive months			75%	67%	80%
Worst month					(2.3%)
Volatility					3.8%
Sharpe ratio					1.17

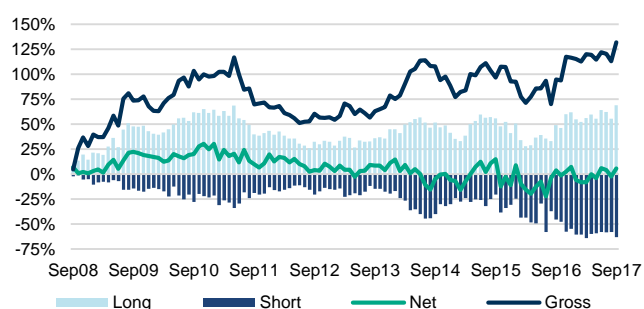
## Monthly key contributors – by sector

Longs	
Positive	Resources, banks, REITs, energy
Negative	Telecommunications, NBF, retail
Shorts	
Positive	Healthcare, transport, resources, REITs
Negative	Banks

## Cumulative performance



## Fund investment profile (% NAV)



## Portfolio settings

% of NAV	Long	Short
Equities	68.8%	-31.7%
Debt/ Hybrids	0%	0%
Derivatives		-31.4%
Gross exposure		132.0%
Net exposure		5.7%
Concentration by position	Long	Short
Top 5	25.1%	(22.3%)
Top 10	43.2%	(31.7%)
Top 15	56.2%	(31.7%)

## Fund strategy and outlook

The Trust's objective is to steadily compound investor returns over time through stock alpha generation, with an overarching focus on capital preservation.

The Trust recorded a solid net return of +2.8% for the month, again demonstrating its ability to outperform for investors when the broader equity market is trading flat to down. (The ASX200A delivered +0.27% gross for the month).

An interesting feature of recent Australian market performance (or lack of it) has been the breakdown in the usually strong correlation with offshore equity markets. Part of this is likely due to currency – the AUD continues to retrace from recent highs. There is plenty of international capital chasing yield in Australian equity (and debt) securities, typically on an unhedged basis. As a consequence, this money is very FX rate-sensitive. Another factor may be the slide in iron ore prices, which is unlikely to give investors comfort on the prospects for our highly indebted household sector as the property bubble peaks. Another factor could be Government. The energy mess is bad enough from a domestic consumer and business perspective, but increasingly erratic policy-making may also impact foreign investor confidence and be additionally unhelpful for markets.

As a manager that focuses constantly on preserving investor capital, there are plenty of risks to take into account. Ultra-low interest rates may continue to underpin expensive equity valuations, but this trade is now very long in the tooth. Absent another growth shock, key offshore central banks seem keen to lift rates and tighten liquidity. In Australia, there seems less immediate upward pressure on rates, but our banks have been tightening credit for some time. We remain wary about the outlook for housing and its broader implications for the economy and the banking sector in particular.

During September, we extended the gross exposure of the Trust to 132%. It remains relatively defensively positioned, with a modest net market exposure at the end of September, at 6% of NAV.

# ARCO Investment Management Absolute Trust

Monthly report: September 2017

## Performance review

The long portfolio drove most of the Trust's performance during September.

The Trust again generated strong returns from our investment in lithium producers – Orocobre, Galaxy Resources and Pilbara Minerals. It proved something of a break-out month for the sector as the news on key demand drivers continued to build, including reports that China is considering a ban on internal combustion vehicles, and that key European car manufacturers are rapidly bringing forward their plans for migration to electronic vehicle (EV) production.

Elsewhere, we continue to favour companies with significant self-help and/or offshore earnings exposure. We began building a position in Brambles this month, in part replacing the recently-divested CSL position (which had moved well ahead of our fair value range). Our long-held investment in CYBG again rewarded investors this month.

We increased our retail REIT exposure during the recent Amazon-inspired sell-off, and this contributed positively to the Trust's return. This was partially offset by our long Harvey Norman exposure (divested during the month), where our hopes for greater financial transparency

and possible capital management were only partially delivered, with an underwhelming market response.

Long positions in Automotive Holdings, Macquarie Bank and Janus made useful contributions for the month. We increased our long position in Telstra during the month, but this remained a drag on overall performance. We moved to exit our investment in Santos, and concurrently closed our short position in Woodside.

Our aggregate short positions again positively contributed to the Trust's performance for the month.

## Absolute Trust – monthly returns

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FY
FY18	0.24%	(0.29%)	2.79%										2.73%
FY17	(2.28%)	0.02%	0.56%	0.35%	0.95%	0.29%	(1.00%)	(0.98%)	0.94%	0.07%	0.17%	1.88%	0.93%
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 15/09/08.

## Absolute trust – distribution history

Y/e June	2009	2010	2011	2012	2013	2014	2015	2016	2017
Series 1 units	\$1.23	\$1.31	\$2.03	\$0.41	\$0.12	\$0.34	\$0.46	\$0.71	\$0.43

## Fund facts

Initial series NAV	\$10.822	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
Firm AUM	\$119m	ISIN	AU60OPT0014
		Fund Inception	15/9/08 (@ \$10.00 per unit)

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 Australia Absolute Trust. Returns and prices are quoted net of all expenses, management fees, and accrued performance fees. 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 Information Memorandum, and the relevant Subscription Application.