To: **Investor Partners of Castlereagh Equity Pty Ltd**

From: **Peter Phan**

Date: **29 April 2016**

Re: **Monthly Update**

	Castlereagh Equity	ASX All Ordinaries	Relative Performance	CE Net Asset Value
1 November 2013 to 29 April 2016	30.3%	-1.9%	32.2%	130.3 cents
1 November 2013 to 31 January 2015	6.2%	2.4%	3.8%	106.2 cents
1 February 2015 to 29 January 2016	19.4%	-9.2%	28.6%	126.8 cents
1 February 2016 to 29 April 2016	2.7%	5.4%	-2.7%	130.3 cents

To aid in understanding the tables above:

1. CE commenced on 1 November 2013 with shares issued at $1 per share, backed by $1 of cash per share.
2. The first row of the table above provides a summary of CE's performance since its commencement on 1 November 2013 until the date of this memorandum. It also compares CE's performance with the benchmark All Ordinaries index over the same period.
3. The second row of the table provides a summary of CE's performance for its first reporting period (15 months period from 1 November 2013 to 31 January 2015).
4. The third row of the table provides a summary of CE's performance for its second reporting period (12 months period from 1 February 2015 to 29 January 2016).
5. The fourth row of the table provides a summary of CE's performance for its third and current reporting period (period commencing 1 February 2016 to the date of this memorandum).

The XAO started at 5420 on 1 November 2013 and ended at 5316 on 29 April 2016. In percentage terms, the XAO dropped 1.9% for the 30 months period since the start of the CE fund. CE's performance over the same 30 month period is 30.3%.

For the month of April 2016, the XAO gained 3.2%. The CE portfolio did not keep pace, gaining less than 1% for the month. During April 2016, we made a few add-on purchases to existing holdings, and sold one of our holdings. Despite our purchases, the cash component of the CE fund is still at 28%.

A Longer Term Perspective

Jeff Bezos, CEO of Amazon, has recently reminded his investors that the current observable outcomes are the fruits of efforts expended two to three years back. This is a timely reminder to both myself and to our investor partners. CE's results to date are predominantly the outcome of ideas germinated two to three years ago. During the last three months, we have deployed capital into several positions where we do not expect our ideas to be validated for at least two to three years, perhaps even five years. We hope to be able to progressively deploy capital over the next two months if the market should present us with good opportunities at a good price. If we do so, we do not expect the new positions to bear fruit for at least 2 to 5 years.

The ability and capacity to be patient is a significant investing edge. Reasonably foreseeable events in the next quarter or half year or within the next 12 months are usually already factored into prices. What we have continually observed is that the market is not interested in waiting for more than 12 months for an event to play itself out. We have a few holdings where we are reasonably certain will be earning 3 times or even 10 times more within 5 to 10 years. Whilst we can never be 100% sure, the upside probability is often given to us without charge, enabling us to carry a “free” lottery ticket, to use a flawed analogy, or more accurately, an option with zero premium. Our main job is then to make sure that we minimise our downside by ensuring that even if we are wrong or unlucky, our losses are limited.

This brings us to the next (yawn-inducing) topic.

Risks and Errors

I have harped on about risks and errors on many occasions. This is because I firmly believe that minimising risks and errors is the key to long term investing success. One can find an analogy in almost every human endeavour- tennis players practising endlessly to avoid hitting the ball out of the court, musicians practising to avoid playing the wrong keys, writers avoiding typos, mathematics students avoiding calculation errors, chefs avoiding wrong ingredients, etc. The list is countless.

It is then perplexing as to why such a perfectly natural and prudent practice is not naturally carried out in share investing.

In managing the CE portfolio, we analyse our mistakes regularly to gain insights in order to avoid repeating them in the future. It is not a simple and straightforward endeavour. When we talk about mistakes, we are referring to mistakes in our process, rather than outcomes. Usually, mistakes result in losing money on a position, for example buying at $1 and selling at 50 cents. On rare occasions, we make mistakes but manage to sell for a gain. This is the most dangerous sort of mistake because it provides false feedback. The sharemarket is tricky with false feedbacks, another example being a situation where there was no mistake in process, and yet the outcome is lousy. This false feedback is also dangerous because it erodes confidence and encourage departure from a correct system or process eg switching systems from value to momentum to technicals to quantitative.

Lastly, the silent killer of the mother mistakes of them all. The mistake of omission, in that a good process was followed and yet no action was taken for reasons unrelated to the process. Mistakes of omission are where big opportunity costs are incurred, such as, for yours truly, selling Commonwealth Bank in 1997 for $13, happy with a 30% gain, and missing out on a multibagger in the two decades following. Also, for yours truly, not buying CSL in 1998, which was a mistake costing over 30x for every dollar I failed to invest in CSL.

A word of warning- I will have much more to say on the topic of risks and errors in future memorandums. Do stay tuned.

Portfolio

The following are brief summaries of some of our major holdings at present:

1. An infrastructure service provider with major tailwinds driven by capital expenditure of the major telecommunications companies and utilities;
2. A small regional bank overseas;
3. A travel solutions retailer;
4. A medical billing and solutions provider;
5. A premium serviced office operator;
6. A small financial planning and funds administration business;
7. A small medical device company;
8. A mobile content distributor and mobile banking solutions provider;
9. A medical diagnostic service company;
10. A cold-chain logistics company.

If any investor partner wishes to contact me to discuss this memorandum or any other matters related to CE, please do not hesitate to do so.

Thank you for your trust and confidence in us.

Regards
Peter Phan
Director, Castlereagh Equity Pty Ltd