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

From: **Peter Phan**

Date: **30 September 2016**

Re: **Monthly Update**

	Castlereagh Equity	ASX All Ordinaries	Relative Performance	CE Net Asset Value
1 November 2013 to 30 September 2016	56.3%	2%	54.3%	156.3 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 30 September 2016	23.2%	9.7%	13.5%	156.3 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 5525 on 30 September 2016. In percentage terms, the XAO increased by 2% for the 35 months period since the start of the CE fund. CE's performance over the same 35 months period is 56.3%.

For the month of September 2016, the XAO was flat. The CE portfolio increased by 1% for the month.

The cash component of the CE fund is roughly 10%.

In my memorandum 12 months ago in September 2015, I wrote that it is important for us to remember that present results are the cumulative consequence of decisions made in the past. This remains very much the case for the CE portfolio over the current reporting season.

With the passage of time, both successes and mistakes are amplified. At CE, I concentrate on identifying mistakes and then weeding them out quickly. This month I continued with some minor weeding by selling another small position where I made a mistake with valuation. Otherwise, I am pleased to advise that the lawn populated by the CE portfolio continues to be in pristine shape.

Thoughts on Franking and Tax Credits Within CE

Investor partners would have recently received CE's Financial Report via email, and some of you would have noted that tax is payable by CE on profits recognised in the last financial year. Once this corporate tax is paid, it gets added to CE's accumulated pool of tax and franking credits. This pool of tax and franking credits equate to roughly 3.4 cents per share.

Our calculation of NAV per share for CE includes tax and franking credits, as these credits can be streamed back to shareholders via franked dividends. However, it is important to note that these credits are not cash, and hence not available to be reinvested for any further gains. My intention has always been to return these credits to investor partners via declaration of fully franked dividends, with the dividends to be automatically reinvested back into CE.

So how do we deal with these tax/franking credits in the event of a redemption? For all practical purposes, due to the existence of these tax/franking credits, a redemption of shares for NAV cannot possibly be an all cash redemption, since the NAV figure includes tax/franking credits, and the latter is not available as cash to be redeemed. We cannot pay a franked dividend selectively to a redeeming shareholder only, as dividends are payable to all shareholders.

At this stage, the only sensible solution that comes to my mind is that investor partners wishing to redeem shares for cash must forgo the tax/franking credit portion of the NAV per share. Conversely, this also means that any remaining investor partners will get the benefit of these tax/franking credits "left behind" by investor partners who have redeemed their shares.

On the other hand, the situation reverses itself in periods when CE has accumulated losses with no tax/franking credits. During these periods, an investor partner will redeem shares for cash for the full NAV value, and the accumulated losses will be "left behind" to be shouldered by remaining investor partners.

Given that we are likely to keep the pool of tax/franking credits to a minimum by paying fully franked dividends, this issue is likely to be of diminishing significance over time going into the future. Nevertheless, the issue cannot be fully eliminated. For example, we may have a fortunate year where we liquidated a significantly large position, and tax paid on the gains will give rise to a large tax/franking credit balance.

Before I proceed with amendment of CE policy regarding tax/franking credits forgone on redemption, I will be grateful if investor partners can provide me with feedback. At this stage, the issue is a hypothetical, as CE has not have a single redemption since inception. We have been blessed with such strong support from our investor partners.

You can contact me by telephone, or you could write to me, whichever way you prefer. Please provide me with your feedback before 28 November 2016. If I decide to proceed with this policy (or otherwise), I will do so at the same time as we publish the November 2016 memorandum.

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