

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

**From: Peter Phan**

**Date: 29 June 2018**

**Re: Monthly Update**

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	Castlereagh Equity	ASX All Ordinaries	Relative Performance	CE Net Asset Value
1 November 2013 to 29 June 2018	61.8%	16%	45.2%	136.8 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 31 January 2017	19.7%	12.5%	7.2%	151.8 cents
1 February 2017 to 31 Jan 2018	9%	8.3%	0.7%	146 cents
1 February 2018 to 29 June 2018	-1.6%	2.3%	-3.9%	136.8 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 reporting period (12 months period from 1 February 2016 to 31 January 2017).
6. The fifth row of the table provides a summary of CE's performance for its fourth and current reporting period (period commencing 1 February 2017 to the date of this memorandum).
7. \*CE NAV is after payment of dividend and director fees in Feb 2017 and Feb 2018. These payments "reset" the NAV from 1.52 to 1.34 in Feb 2017 and from 1.46 to 1.39 in Feb 2018.

The XAO started at 5420 on 1 November 2013 and ended at 6290 on 29 June 2018. In percentage terms, the XAO gained 16% for the 55 months period since the start of the CE fund. CE's performance over the same 55 months period is 61.8%.

For the month of June 2018, the XAO was 2.7%. The CE portfolio was flat for the month.

The cash component of the CE fund is just under 29% as we deployed funds incrementally into our existing positions. 3 of our positions are now the subject of M & A activity, and most of my time in June has been spent on researching and working out the best course of action in respect of our holdings.

### **Growth and Momentum Continue to be Sexy**

This has been a period of underperformance for value funds such as CE. We are now trailing our benchmark by nearly 4%. Exactly 12 months ago, in our memorandum of June 2017, I stated that RWC was trading at a market cap of \$1.8b which was about 23x earnings. At close of trading today, RWC was trading at a market cap of \$4.2b, at about 35x earnings. An investor buying RWC shares at precisely 12 months ago when I deemed it too expensive would be sitting on nearly 70% gains at the end of today.

The same story is replicated with the other two stocks I mentioned, namely CSL (up 36%) and COH (up 25%). The story is similar for all of the usual market darlings at present- NWL, XRO, NAN, APT, APX, ALU, etc. The major theme playing out appears to be a direct copycat of the FAANG stocks in the USA- a preference for global growth businesses in the software/technology sectors, irrespective of price. On top of indiscriminate buying by index funds, not being in these stocks would also have been a major career risk for active fund managers as they would be underperforming their benchmarks.

Value investing works precisely because it does not work all the time. This is precisely such a time. Historically, over the last 100 years, there have been 3 other major periods similar to the present- the Great Depression 1930s, the oil shock 1970s, and the tech boom 1990s. I am not convinced of any fundamental reason as to why the current state of momentum chasing should persist indefinitely. So this too shall pass, although plenty of patience would be tested from now until then.

Thank you for your trust and confidence in us.

Regards

Peter Phan

Director, Castlereagh Equity Pty Ltd