

# Merlon Australian Share Income Fund



## Monthly Fact Sheet – October 2017

For queries, please call Adviser Services on 1800 195 853

| Performance <sup>i</sup> (%)    | Month | Quarter | FYTD | Year | 3 Years (p.a.) | 5 Years (p.a.) | 7 Years (p.a.) | 10 Years (p.a.) |
|---------------------------------|-------|---------|------|------|----------------|----------------|----------------|-----------------|
| Fund Total Return (net of fees) | 1.0   | -0.4    | 0.9  | 11.8 | 7.8            | 10.9           | 8.8            | 5.1             |
| ASX200                          | 4.0   | 5.2     | 5.2  | 17.6 | 8.4            | 11.8           | 9.7            | 4.7             |
| Average Daily Exposure          | 69%   | 68%     | 68%  | 68%  | 69%            | 69%            | 70%            | 72%             |
| Gross Distribution Yield        | 0.5   | 1.9     | 2.4  | 7.4  | 7.6            | 7.9            | 9.1            | 9.2             |

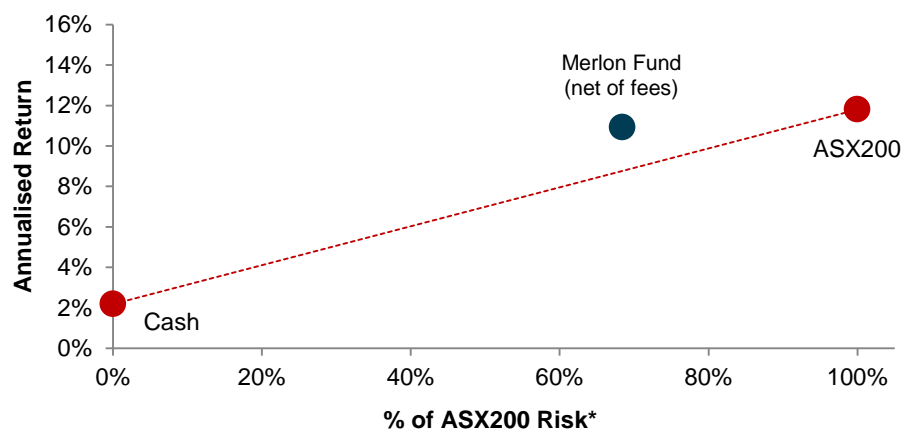
\* Past performance is not a reliable indicator of future performance. All returns above are grossed up for franking credits. Portfolio inception date is 30/09/2005.

### Monthly Performance Commentary

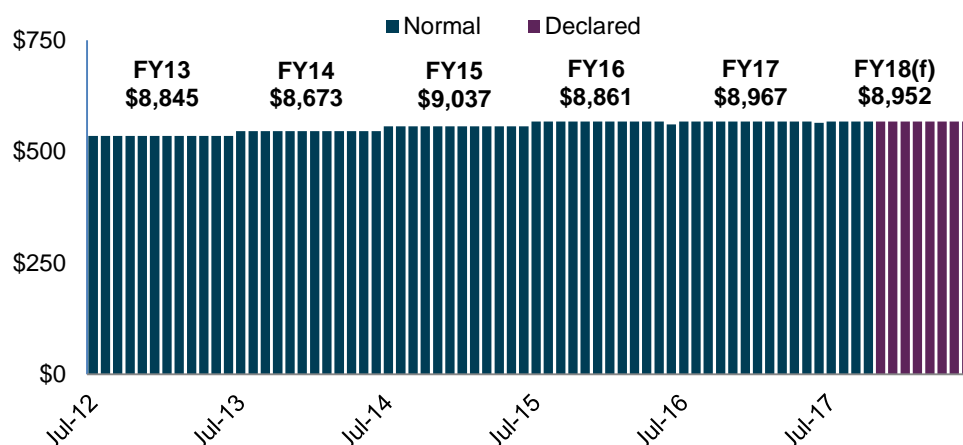
The ASX200 rallied strongly in October, retuning 4% for the best monthly return of the year. The gains were broad based, with all sectors recording positive returns. Energy and Consumer companies were the best performers whilst Financials and Materials contributed half the total index gain during the month. Telecommunication companies and Real Estate Investment Trusts were the worst performers, albeit still providing small positive returns.

The Fund returned 1.0% for the month, underperforming the ASX200. Fletcher Building detracted the most after announcing further losses on problem construction contracts. Consumer companies, Trade Me and Sky Television, also detracted, as did Magellan Financial. The hedge overlay also reduced returns as expected given the strong market. The best performers for the Fund in the month were, NewsCorp, Origin Energy and QBE Insurance.

### Rolling Five Year Performance History<sup>ii</sup>



### Monthly Income from \$100,000 invested in July 2012<sup>iii</sup>



### Top Ten Holdings (%)

|                  |     |
|------------------|-----|
| Caltex           | 5.3 |
| Westpac          | 5.2 |
| Origin Energy    | 5.1 |
| Coca Cola Amatil | 5.1 |
| ANZ Bank         | 5.1 |
| News Corp        | 5.0 |
| Woolworths       | 4.9 |
| Suncorp Group    | 4.9 |
| AMP              | 4.9 |
| Wesfarmers       | 4.9 |

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| Fund Details           |                   | Portfolio Analytics <sup>iv</sup> |             |               |
|------------------------|-------------------|-----------------------------------|-------------|---------------|
| Fund size              | \$ 523m           |                                   | <b>Fund</b> | <b>ASX200</b> |
| Firmwide FUM           | \$ 1,552m         | Number of Equity Positions        | 27          | 200           |
| APIR Code              | HBC0011AU         | Active Share                      | 75%         | 0%            |
| ASX Code               | MLO02             | Net Equity Exposure               | 69%         | 100%          |
| Inception Date         | 30 September 2005 | Beta                              | 0.7         | 1.0           |
| Distribution Frequency | Monthly           | EV / EBITDA                       | 9.0x        | 12.0x         |
| Minimum Investment     | \$ 10,000         | Price / Earnings Ratio            | 15.0x       | 17.2x         |
| Buy / Sell Spread      | +/- 0.20%         | Trailing Free Cash Flow Yield     | 5.7%        | 4.9%          |

## About Merlon

Merlon Capital Partners is an Australian based fund manager established in May 2010. The business is majority owned by its five principals, with strategic partner Fidante Partners Limited providing business and operational support.

Merlon's **investment philosophy** is based on:

**Value:** We believe that stocks trading below fair value will outperform through time. We measure value by sustainable free cash flow yield. We view franking credits similarly to cash and take a medium to long term view.

**Markets are mostly efficient:** We focus on understanding why cheap stocks are cheap, to be a good investment market concerns need to be priced in or invalid. We incorporate these aspects with a "conviction score"

## About the Fund

The Merlon Wholesale Australian Share Income Fund's investment approach is to construct a portfolio of undervalued companies, based on sustainable free cash flow, whilst using options to overlay downside protection on holdings with poor short-term momentum characteristics. An outcome of the investment style is a higher level of tax-effective income than the broader market, paid monthly, along with the potential for capital growth over the medium-term.

## Differentiating Features of the Fund

**Deep fundamental research** with a track record of outperformance. This is where we spend the vast majority of our time and ultimately how we expect to deliver superior risk-adjusted returns for investors.

**Portfolio diversification** with no reference to index weights. The benchmark unaware approach to portfolio construction is a key structural feature, especially given the concentrated nature of the ASX200 index.

**Downside protection** through fundamental research and the hedge overlay. In addition to placing a heavy emphasis on capital preservation through our fundamental research, we use derivatives to reduce the Fund's market exposure and risk by 30% whilst still retaining all of the dividends and franking credits from the portfolio.

**Sustainable income**, paid monthly and majority franked. As the Fund's name suggests, sustainable above-market income is an outcome of our investment approach and a key objective of the Fund.

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## Footnotes

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### <sup>i</sup> Performance (%)

*Average Daily Market Exposure* is calculated as the daily net market exposure divided by the average net asset value of the Fund.

*Fund franking:* Month 0.1%, Qtr 0.6%, FYTD 0.6%, Year 1.5%, 3 Years 1.8% p.a., 5 Years 1.8% p.a., 7 Years 2.1% p.a., 10 Years 2.3% p.a.

*ASX200 franking:* Month 0.0%, Qtr 0.5%, FYTD 0.5%, Year 1.5%, 3 Years 1.5% p.a., 5 Years 1.5% p.a., 7 Years 1.5% p.a., 10 Years 1.5% p.a.

### <sup>ii</sup> Rolling Five Year Performance History

Past performance is not a reliable indicator of future performance. Returns for the Fund and ASX200 grossed up for accrued franking credits and the Fund return is stated after fees as at the date of this report. Merlon Wholesale Australian Share Income Fund franking 1.8% p.a., ASX200 franking 1.5% p.a. % of ASX200 Risk represents the Fund's statistical beta relative to the ASX200

### <sup>iii</sup> Monthly Income from \$100,000 invested in July 2012

Past performance is not a reliable indicator of future performance. Income returns exclude 'bonus income' from above-normal hedging gains of \$849 in FY13 and assume no bonus income in FY17 estimate. Income includes franking credits of: \$2,420 (FY13), \$2,120 (FY14), \$2,356 (FY15), \$2,057 (FY16), \$2,159 (FY17) and \$2,142 (FY18 estimate).

### <sup>iv</sup> Portfolio Analytics

Source: Merlon, Active share is the sum of the absolute value of the differences of the weight of each holding in the portfolio versus the benchmark, and dividing by two. It is essentially stating how different the portfolio is from the benchmark. Net equity exposure represents the Fund's net equity exposure after cash holding's and hedging. Beta measures the volatility of the fund compared with the market as a whole. EV / EBITDA equals a company's enterprise value (value of both equity and debt) divided by earnings before interest, tax, depreciation, and amortization, a commonly used valuation ratio that allows for comparisons without the effects of debt and taxation.

## Disclaimer

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