Monash
ABSOLUTE INVESTMENT FUND

Monthly Performance Report

August 2016

Fund Strategy

The Monash Absolute Investment Fund ARSN 606 855 501 (Fund) offers investors an Australian equity fund that aims to deliver high absolute returns of 12-15% p.a. (after fees), over a full investment cycle and preserve investor capital each financial year.

The Fund is benchmark unaware, style and stock size agnostic, both long and short and only invests in compelling opportunities. In keeping with the Fund's absolute return objectives, if the team cannot find stocks that meet the very high return hurdle requirements, the Fund will preserve that capital in cash at bank.

Monthly Update

The Fund was down 1.11% (after fees) for the month of August, during which the equities market was also weak. The S&P/ASX200 fell 1.59% for the month.

The key contributors for the month were stocks the Fund held in medical device companies and retailers. The medical device companies are making good progress. Airxpanders (ASX: AXP) rose 20% after presenting at a broker's conference and Impedimed (ASX: IPD) was up a further 15% following the FDA's positive announcement regarding Digital Health. The retailers were Kogan (ASX: KGN) which rose 15% exceeding its Prospectus forecasts, Lovisa (ASX: LOV) was up 13% as its U.K. store roll out accelerated, and Harvey Norman (ASX: HVN) was higher by 11% with strong sales and margins.

The Fund had two key detractors this month. G8 Education (ASX: GEM) was down 20% on weaker margins and the Fund's short position in Insentia (ASX: ISD) was up 21% due to a strong outlook, before the Fund covered. Together these cost the Fund's portfolio over 2%, with the remainder of the Fund's holdings, on balance, doing well.

Monthly Portfolio Metrics

Outlook Stocks (Long)	21 Position: 69%
Outlook Stocks (Short)	1 Positions: -3%
Event, Pair and Group (Long)	5 Positions: 14%
Event, Pair and Group (Short)	1 Positions: -3%
Cash	23%
Gross Exposure	89%
Net Exposure	77%
Beta	0.50

Return Summary Since Inception[1]

Since Inception (p.a.)	13.70%
1 Month	-1.11%
3 Months	-3.07%
6 Months	3.56%
FYTD	0.80%
1 Year	7.22%
2 Years	5.36%
3 Years	10.40%
Cumulative	70.72%

[1]Inception date of Fund is 2 July 2012.

Portfolio Analytics Since Inception

Sharpe Ratio	1.22
Sortino Ratio	2.66
Standard Deviation (p.a.)	9.02%
Positive Months	64%
Maximum Drawdown	-7.71%
Avg Gross Exposure	88%
Avg Net Exposure	77%
Avg Beta	0.58
Avg VAR	1.17%

Key Fund Information

FUM	$36m
Minimum Investment	$20,000
Management Fee	1.53% p.a.
Performance Fee	20.5% above the RBA Cash Rate with High Water Mark
Pricing Frequency	Daily
Distributions	Annually
APIR Code	MON0001AU
Morningstar Category	Alternatives Strategies

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Retailers Ramping Up

Retailers are a sector of the market whose earnings are difficult to forecast accurately. They are prone to surprise the market more than any other sector each reporting period. During the reporting month of August just passed, 10 went up more than 5% in price on the day of their result, and another 10 fell more than 5% on the day.

Retailers' profits are generally less predictable than other companies because small variations in their volumes and selling prices typically result in large variations to their profit margins, and it is hard for an outside observer to know what is going on with the quantity and mix of products sold and the prices at which they are selling them.

On the other hand, there are times when retailers can deliver strong growth in earnings over an extended period. This is evident when a firm rolls out a network of stores that are rapidly profitable (think the early days of Flight Centre or Harvey Norman) or whose customers are demanding more products that have high margin and high turnover (like JB Hi-Fi as it replaced floor space for records and musical equipment with consumer electronics).

Lovisa

Lovisa is a stock that the Fund holds that has a long runway of store roll out opportunities ahead of it.

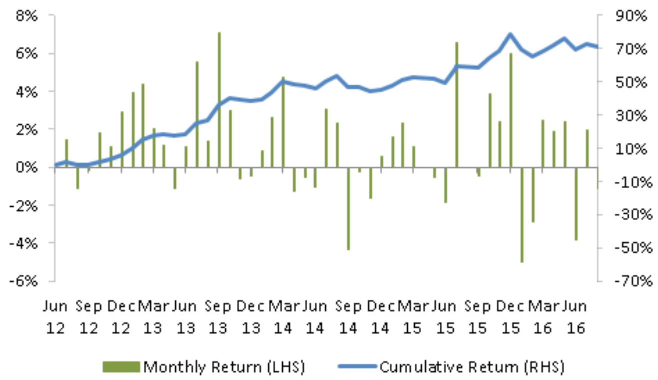
Lovisa retails low cost jewellery as fast fashion. The customers are principally young women who want the latest accessories to wear with their clothes. Lovisa has addressed this market by designing its own product, based on the latest trends from social media and fashion shows. Lovisa aims to replenish 15% of their inventory each week with new designs so there is always something new to see in store. The stores have a relatively small footprint, yet high turnover.

This contrasts with fashion stores that are focusing on a wider demographic with a wider range of price points. Competitors often have accessories as a smaller part of apparel stores but do not specialise in it. The speed of Lovisa's inventory cycle is unique for a specialist jewellery company as some competitors have inventory cycles of 3 months plus. However, Zara operates with a similar inventory cycle to Lovisa in the apparel sector.

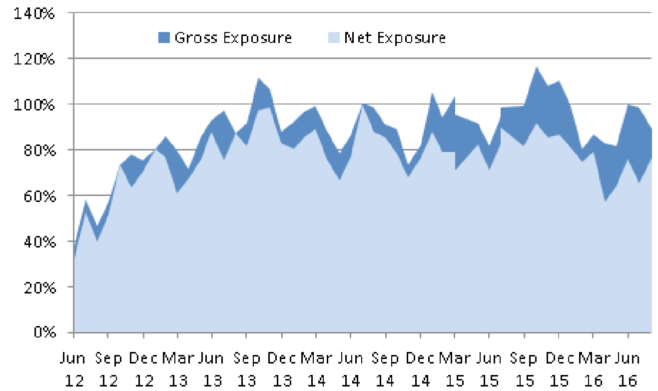
The business model was rolled out rapidly in Australia where they have 145 stores and it is mature. However, they are only at the beginning of their international store roll out, which accounts for 36% of group sales. Locations include New Zealand, South East Asia, the Middle East and South Africa. Critically, all of these international operations have a similar return profile as Australia, demonstrating that this store format works across different international markets. They have 4 stores in the UK, and this is to be a particular focus of growth going forward following the success of their pilot program, which only started in November 2015.

The payback on a new store is between 4 and 8 months, with same store sales growth of around 4%pa. Given these exceptional returns on invested capital Monash Investors' view is that there is little doubt that Lovisa's management and Board will materially expand its store network. The size of the UK market is such that the store rollout in this market alone could easily double profits over time, and then there is Europe and the USA to consider. With Lovisa trading at a valuation discount to other retailers and with a dramatically greater growth runway, Monash Investors' view is that the there is significant upside to the share price.

Cumulative Return Since Inception



Gross/Net Exposure Since Inception



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Kogan

Internet retailing has been one part of the market that has taken a bit of a beating lately, for example, Surfstitch, Temple & Webster and AHA Life. The Fund did not invest in any of these so it was good to see a company in which the Fund did invest, Kogan, beat its prospectus forecast quite strongly.

Kogan started out as an on-line retailer of consumer appliances/electronics and has expanded into many other product lines, selling big brands as well as its own private label. It listed in order to raise capital to accelerate the growth of its private label range, which provides a higher margin than selling the brands of other manufacturers.

The Kogan result beat its prospectus revenue and margin forecasts solidly, and they continue to enjoy an increase in on-line visits of over 20% pa. While they will not be giving guidance until their AGM, a mix change towards more private label and higher margin verticals should further support a strong outlook.

Harvey Norman

Harvey Norman was in the Fund portfolio during August as an Event[i] trade – the catalyst being its upcoming earnings result.

Harvey Norman is a business that has revenues and margins that are sensitive to building activity, for example bathroom, kitchen, appliance, and furniture sales. It is also a big seller of consumer electronics. When times are good, the percentage margin paid to its franchisees is narrowed, exaggerating the profit uplift to Harvey Norman (and when times are bad franchisees are subsidised).

Monash Investors saw that this reporting season was headed for a very good result for Harvey Norman for two reasons. Firstly, there had been extremely strong building activity. Secondly, with the collapse of Dick Smith, competition had lessened in consumer electronics.

The result played out the way the Monash Investors thought it would, and the stock rose and it largely beat expectations and then rose further again on the day of the result. The stock was then exited.

[i] Event means securities that Monash Investors has identified a near term event or catalyst that it believes should drive a share price reaction.

[ii] Outlook means securities that in Monash Investors' view whose current valuation does not reflect the future earnings potential of the business.

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