

**Investment Performance**

As at 30 June 2018	Feb	March	April	May	June	Cumulative
Indian Pacific Fund (after fees)	1.03%	-1.18%	2.11%	-0.20%	1.61%	3.34%
ASX All Ords Accumulation Index	0.18%	-3.55%	3.49%	1.40%	2.95%	4.39%

**Month end exposure**

Long Exposure	92%
Short exposure	-12%
Gross exposure	105%
Net exposure	80%
Cash Weight	20%

**Portfolio Positioning (net)**

Fund	ASX300^	Difference	
Consumer Discretionary	16.4%	5.0%	11.5%
Consumer Staples	12.5%	8.1%	4.4%
Energy	0.0%	5.8%	-5.8%
Financials	34.2%	32.6%	1.6%
Health Care	3.9%	8.4%	-4.5%
Industrials	0.8%	7.2%	-6.4%
Information Technology	3.3%	2.5%	0.8%
Materials	3.9%	18.5%	-14.6%
Real Estate	-3.0%	7.7%	-10.8%
Telco	0.0%	2.2%	-2.2%
Utilities	0.0%	2.0%	-2.0%
Other	7.7%	0.0%	7.7%
Cash	20.3%	0.0%	20.3%
Number Holdings (both long/short)	34	302	-268

**Top 5 Holdings**

	% Fund
MACQUARIE GROUP LTD	8.0%
WESFARMERS LTD	7.3%
KINA SECURITIES LTD	7.2%
EQT HOLDINGS LTD	5.1%
EVENT HOSPITALITY AND ENTERT	5.0%
Top 5 Holdings as % AUM	32.7%

^based off ASX300 Vanguard ETF (Bloomberg VAS AU Index)

**MONTH IN REVIEW**

The Fund returned +1.6% in June taking cumulative net performance for the first five months to +3.34%, with average net exposure since inception at 63.0%. Average gross capital invested on your behalf in June was 82.4% Long, and 13.4% Short, giving net 69.0% exposure to the market. As you will see above, this increased briefly at month end ahead of some July inflows.

Best individual Long contributors in June (in absolute dollar contribution terms) were again the two biggest holdings in the fund, **Macquarie Group Ltd** and **Wesfarmers Ltd** which ran in tandem +8%. Whilst both have likely found their level for the time being they each have multiple growth levers to pull in the years ahead and neither look expensive versus the market or their domestic peers, hence we will maintain exposure to both companies. Other noteworthy positive contributors for the month were diagnostics imaging business **Capital Health Ltd** (+10%), and **APN Outdoor Group Ltd** (+10%) which received a takeover bid by French company **JCDecaux SA** (albeit a fairly underwhelming bid price in our view).

**Kina Securities Ltd** was added to the fund in June as part of the Fu Shan sell down at 75c. Kina is a PNG based banking and financial services company who I have been following since their IPO in 2015. After meeting them and doing the work in 2015, I decided against investing as their net interest margin (NIM) was well above peers (hence there appeared some downside risk) and I wanted to see more of a listed track record develop given the potential sovereign risk. Three years down the track they have largely "done what they said they would" – loan growth has been very strong, NIM has drifted a bit lower, asset quality tests point to a reasonable quality bank book, and Wealth Management has been growing nicely. For these reasons the stock has been on my watch list since starting the fund. Last month two significant events occurred. Firstly, Kina announced they were buying ANZ's PNG Retail and commercial/SME business for a giveaway price of 2x FY17 earnings (ANZ are exiting retail in much of Asia and Kina were effectively the only buyer the regulator would allow to acquire it). The acquisition effectively doubles their market share and gives them access further liquidity from ANZ's book which has a deposit to loan ratio of over 200% (versus Kina at 74%). In PNG, where 70% of the population are still not banked, there are no shortage of loan opportunities (20-30% loan growth is the norm), it's more about accessing liquidity and lending responsibly. So the additional liquidity is very important as it will significantly boost Kina's ability to lend. The acquisition is 30% accretive on an FY17 pro forma basis, and after reviewing every single loan with their auditor Kina are not taking any problem loans plus they have further protection with ANZ agreeing to cover 50% of any losses on their book for two years after deal closure (3Q 2019).

The second significant event last month was the forced sell down by founding shareholder Fu Shan, who rightly or wrongly, had perceived governance issues. Fu Shan's exit frees up stock liquidity and opens the way for three more independent directors to join the board. We understand the exit of Fu Shan has already seen some customers increase their desopits with Kina significantly, plus it will make it much easier for Kina to form corresponding bank partner relationships (allowing FX income in particular to grow). During the month we did a call with the Kina CEO in Port Moresby, Greg Pawson, who is a very well qualified bank executive with a strong resume. We also did a call with an ex Kina board member and an independent bank contact in the PNG to ensure we were over the issues. At the placement price of 75c we bought Kina stock on 5.0x FY19 earnings, with a forecast yield of 15%. Post the ANZ accretion, on an FY20 basis, the multiple is more like 3.5x. Whilst recognizing the market cap is small and there will always be a "sovereign discount", if they can deliver on their plan we see no reason KSL shouldn't rerate to 7-8x FY20 earnings in the next 12-18 months, which is over \$1.50.

On the downside in June, whilst we don't currently hold any pure mining producers, mining service name **Mineral Resources Ltd** (MIN, -13%) had a poor month after they downgraded their expectations for Direct Shipping Ore (DSO) export volumes from their Wodgina Lithium mine (the largest known hard rock lithium deposit in the world based on JORC Resource). DSO revenue effectively comes from low grade (circa 1.5% lithium) pre-strip ore which would normally be worth very little (rather, it was filling a temporary supply gap before higher grade product comes online). The fund reduced its position in MIN in early June at higher levels because soft monthly port export data pointed to it being tough for MIN to meet DSO guidance, however with the stock now trading around \$15.00 the market appears to have over reacted in our view by applying a multiple to the P&L impact, even though the DSO revenue stream was always due to cease after 2019. Whilst not entirely comfortable with the volatility in the MIN share price or with the commodity price exposure, we are attracted to their business model of using their intellectual property to build long term mines and then drive down production costs before selling down their equity stakes, whilst retaining the steadier mining service revenue streams with life of mine operating contracts (often 20-30 years). True to strategy, they are currently running a process to sell 49% of Wodgina which could yield a significant sum (circa \$1bn+ in cash has been speculated versus current \$2.8bn market cap). There are still likely some downgrades to wash through the markets FY19 estimates which might keep a lid on the share price as short term, however with MIN now trading on around 6x FY19 free cash flows (on our below market estimates), the stock represents good long term value.

**Shorts** made a small positive contribution overall for the month with two core retail shorts dropping 8-10%, a telco position dropping 7%, and a hospital operator down 12%. Rate sensitives however had a stronger month with many going ex-dividend which detracted from gains on the short side.

Reflecting on the funds first five months in existence I am happy with how things are placed. To date, I think most of you understand that capital preservation has been front of mind. Looking ahead to our first clean financial year in FY19, the key focus is to find opportunities to deploy our cash into attractively priced long term investments. Operationally within the business everything is running smoothly with our outsourced service providers all performing their roles well (Morgan Stanley on Prime Brokerage and Custodian, Attentus on back and middle office, Apex on Fund Administration, BDO on tax and audit, and Norton Rose on legal).

After travelling to Melbourne last month, and with much of the market in "blackout" ahead of reporting season, I am back in Sydney this week seeing both buy and sell side contacts which should contribute further to idea generation.

#### About the fund:

The Indian Pacific Fund is an Australian Equity long/short fund founded in February 2018. The fund has an absolute return focus (with long bias), has no cash limit, and can invest in both large and small cap companies. The investment process is a fundamental bottom up investment process with a focus on balance sheet risks and identifying companies with strong cash flows, in good industries, with strong management teams. The fund was founded with the view that whilst markets rise in the long term it is prudent to maintain the flexibility to hold more cash when markets are overly optimistic, and selectively short stocks if opportunities arise.

<b>Holdings</b>	Typically 15-25 long, selective short positions	<b>Investor Eligibility</b>	Wholesale Clients
<b>Management Fee</b>	1.0% of the GAV of the Fund, plus GST	<b>Prime Broker/Custodian</b>	Morgan Stanley
<b>Performance Fee</b>	20% of Outperformance over RBA Cash, high water mark	<b>Fund Administrator</b>	Apex Fund Services Ltd

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