MONTAKA GLOBAL ACCESS FUND
QUARTERLY LETTER

MONTAKA

JUNE 2016

UNIT PRICE # **$0.9181**

FUND COMMENTARY

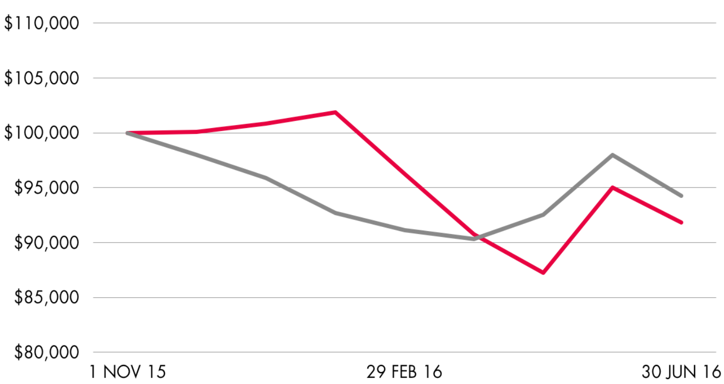
In the month of June, the Montaka Global Access Fund declined by 3.35%, net of fees, driven in large part by a 3.01% increase in the Australian dollar, relative to the US dollar. For the June 2016 quarter, the Fund increased by 1.17%, net of fees. Since inception on 1 November 2015, the Montaka Global Access Fund was down 8.19%, net of fees, versus the global market[2] which was down by 5.73% over the same period, in Australian dollar terms.

The June quarter was another highly volatile period in the global markets, particularly when viewed in Australian dollar terms. The quarter started out with a continuation of the coordinated stimulus efforts from major economy policymakers, led by China. The quarter ended with a surprise "Brexit" vote by the citizens of Britain, sparking a global financial market selloff.

The Chinese stimulus efforts marked a return to an acceleration of State-backed fixed-asset investment that had characterized much of the last decade. Of course, it has been this exact recipe that has led to a significant build-up in poor credit-quality loans over the years within China's banking system. So what to make of China's new stimulus effort? Patrick Chovanec, a leading economist and observer of the Chinese economy, summed it up best when he tweeted the following: "It shows signs of a tiny and unsustainable debt-fuelled bump which will only make things worse in the end = recovery?"

Notwithstanding, the combination of increased fixed-asset investment by Chinese State-backed entities with a temporary abandonment of tightening monetary policy in the US led to a sudden compression of credit spreads and a sharp rally in stocks of low quality businesses. The prospect of "free and easy" money forever meant that highly indebted businesses were thrown a lifeline which increased the market value of their equity.

FUND PERFORMANCE[1]



1) Inception: 1 November 2015
2) MSCI World Net Total Return Index in Australian dollar terms

PERFORMANCE ATTRIBUTION (%)

	June 2016
Long portfolio contribution	(0.28)
Short portfolio contribution	(0.06)
Change in AUD/USD	(3.01)
Net return	(3.35)
Since inception[1]	(8.19)

EXPOSURES* (as at 30 June 2016)

	% of NAV
Long exposure	99.0
Less: short exposure	(45.3)
Net market exposure	53.7

POSITION METRICS* (as at 30 June 2016)

	Long Portfolio	Short Portfolio
Number of positions	24	36
Largest position size	7.2	1.9
Smallest position size	2.1	0.5
Average position size	4.1	1.3

Note: sizes shown as % of NAV

TOP 10 LONG POSITIONS* (as at 30 June 2016)

		% of NAV
1	Playtech	7.2
2	REA Group	6.9
3	Insperity	5.6
4	Essilor	5.4
5	Foot Locker	5.3
6	CVS Health	5.2
7	Apple	5.2
8	Ross Stores	5.1
9	Aetna	4.4
10	Take-Two Interactive	4.3
	Total top 10 long positions	54.7

FUND SIZE (NAV) ($M) (as at 30 June 2016)

Montaka Global Fund	137
of which: Montaka Global Access Fund	56

* *all exposures, metrics & positions are derived from the underlying investment fund*
 # The fund is forward priced; you will receive the price struck subsequent to the receipt of your application/ redemption request.

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What made matters even more difficult for Montaka's strategy was that, at the same time, stocks of high quality businesses barely moved, or even decreased. In effect, the month of April was characterized by a mass rotation out of quality into junk. We do not pretend to fully understand the drivers of this rotation, though we know that a significant share of daily global trading is conducted by software algorithms that chase momentum – irrespective of the underlying fundamentals of the individual businesses being bought and sold.

Montaka is a strategy that refuses to buy junk and typically will not short quality. On this basis, the June quarter was particularly challenging. Indeed, the only way to do well during a junk rally is simply to own the junk. And we will not do that. We know that, over the medium term, quality acquired at the right price will materially outperform junk.

The quarter finished with an unexpected shock that will likely go down in history as the most politically-significant day in the life of the current generation of Britons. On a cold and rainy day on June 23, Britain held only the third referendum in its history to decide whether or not to remain in the European Union (EU). As we all know, the "Leave" vote won a narrow victory.

The surprise result of the referendum had immediate consequences. The Pound Sterling collapsed by more than 10% in a matter of hours. Friday June 24 marked the largest one day decline in the pound we have ever seen. The panic spread around the world: by that afternoon, the global market closed down by 4.9%.

The turmoil was not restricted to financial markets. British Prime Minister, David Cameron, announced his resignation. At least 10 senior members of the opposition party resigned from the shadow cabinet calling for Labour leader, Jeremy Corbyn, to resign. And EU leaders scrambled to work out how they should treat the British in light of this referendum result.

While we have little ability to accurately forecast long term political consequences, we believe this referendum will likely leave a significant mark on the EU. At worst, this vote could well mark the beginning of the end of the EU as we know it today. The break-up of the bloc would be extremely disruptive to financial markets. Alternatively, it may well be the case that Britain does not actually leave the EU, despite its referendum. While Britain will surely try to leave the EU, it will almost certainly prove to be an extremely complex, time-consuming and costly process. At some point, the electorate may overwhelmingly swing back to a "Remain" position. The referendum was not legally binding, after all.

The "Brexit" event, as it has become known, tested all investment managers in their risk management capabilities. The concept of risk is both subtle and often poorly understood. It is basically the idea that, while a number of things could happen, only one will happen.

In the days, weeks and months leading up to the British referendum, investment managers were faced with a binary scenario under which only one of two things would happen: (i) Remain would win; or (ii) Leave would win. The former would likely result in a Pound Sterling and equity market rally; and the latter the opposite.

Many investors and pundits spent considerable time and effort trying to assess the probabilities of such outcomes. Polls were commissioned, betting markets analysed and expert opinions sought. At Montaka, we did none of the above. In our view, this exercise was futile. There was clearly going to be an outcome; and one of the possible outcomes was likely going to be highly negative. This is all we needed to know to conclude that we did not want to be exposed in any meaningful way – even if this meant we would miss some of the upside of a potential Remain result.

Prior to the referendum, we exited one UK-based fund manager completely, we dramatically reduced our exposure to another UK-based wealth manager and we hedged the Sterling exposure on substantially all of our UK exposures. Furthermore, we were well positioned to add to certain UK and European names in the event opportunities presented themselves in the days following the result.

The actions described above would certainly have "cost" our investors some of the upside that would have stemmed from a Remain victory. But in return, these actions significantly protected the downside from a surprise Leave result. As our investors know well, Montaka's primary objective is always to protect the downside wherever possible. In footballing terms, we would always pick a superstar goalkeeper before a superstar striker. And this philosophy led to significant outperformance by Montaka over the Brexit period.

Now, despite the significant volatility and global risks that have been described above, we continue to identify individual businesses that stand out as fantastic investment opportunities. Insperity (NYSE: NSP) is one these businesses.

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CASE STUDY: Insperity

Insperity is a US based business that has been around for approximately thirty years. When we started looking at the business earlier this year, it was a relatively small US$900 million company – a size which often rules it out of consideration sets for many large global fund managers. Today, the business is worth US$1.4 billion – and Montaka's flexibility to invest across geography, industry and size allowed us to take advantage of this fantastic growth.

Insperity is essentially a "professional employer organization" which means it acts as the co-employer of the staff of leading small and medium sized businesses across multiple industries and regions within the US. Insperity manages certain human resource-related processes such as payroll, compliance and health insurance on behalf of its clients. And in return, Insperity will take a cut of the staff's wages. Simple enough.

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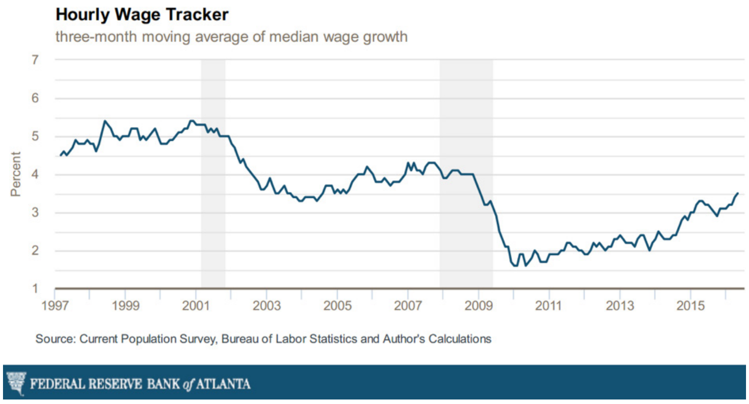
Now, we know that wage growth has been accelerating in the US over recent years, as illustrated below. Indeed, it was for this very reason that the Federal Reserve increased interest rates in December for the first time since 2006. Given that Insperity's revenues are a function of employer wages, it will be one of the few businesses to benefit from this structural trend. As wage growth accelerates, so too should Insperity's gross income.



Yet Insperity is not simply a play on US wage growth – though we do position our global portfolios in line with our observations of what is happening in the world. Insperity's rapid growth in value can be attributed to a sharp improvement in marketing strategy and productivity.

In recent years, Insperity's management team has invested heavily in the business' sales and marketing team and systems. Leads and attachments are tracked and analysed in an intelligent way to generate insights to improve sales productivity. While it has taken a number of years to build out, the investment is now bearing fruit. Cross-selling attachments have increased as have referrals to new clients; retention rates have increased; and training time of new sales staff has reduced significantly. Insperity has become smarter with maximizing return-on-investment of advertising spend; and has even been successful in building out a mid-market offering to remain relevant with their clients as they grow.

The above success in sales and marketing results in higher client growth which, combined with accelerating wage growth, generates higher top line growth for Insperity. The operating costs of the business are reasonably fixed, excluding the recent ramp-up in sales and marketing investment, which creates the exciting prospect of expanding profit margins going forward.

There is no debating Insperity's business quality. When we started looking at the business, Insperity's return on equity was north of 20% (it is much higher now); it was in a net cash position; and generated significant free cash flow – even in excess of its earnings.

We acquired Insperity on the basis of three key factors:

- Insperity was a business of high demonstrated quality;
- We believed Insperity's quality was set to improve further following its investment in its sales and marketing division and its attractive positioning in the US economy to take advantage of rising wages; and
- Insperity was materially undervalued.

On this latter point, we think about valuation primarily in terms of the difference between our expectations for the future profitability of a business; and those expectations implied by the current stock price. Said another way, we need to be clear about our variant perception compared to the market.

When we started looking at Insperity, our analysis suggested that the market was implying approximately five percent top line growth for the business over the medium term. Yet at the time, growth had been running at an average of nine percent per annum. And, given the renewed investment in sales and marketing capabilities, we had every reason to believe the risk in revenue growth would be to the upside. On this basis, we believed expectations built into the stock's price at the time were way too conservative. Fast forward to the first quarter of 2016 as reported in May: Insperity's top line grew by 16%!

Since then, the stock has rallied over 60% and we have trimmed our position somewhat. That said, we still believe there is meaningful upside left in the stock. While the first leg-up was driven by top line growth, we believe subsequent upside will be driven by profit margin expansion.

* * *

While the Montaka Global Access Fund was launched on 1 November 2015, this letter marks the one year anniversary of Montaka's life. To remind readers the Montaka Global Access Fund feeds directly into the Montaka Global Fund and their monthly returns are virtually identical. On the day Montaka launched, Greece defaulted on its IMF loan. Since then, we have faced a surprise Chinese currency devaluation, the first US interest rate hike in a decade and now, of course, a surprise Brexit vote. While we are primarily fundamental, bottom-up investors, no investor can escape the volatility that stems from these globally-significant macro events.

A corollary of the above is that Montaka's month-to-month returns can and will be volatile. This volatility is exacerbated further by the sharp changes in the Australian dollar. But volatility is not risk, in our view. Our view of risk relates to the probability of permanently impairing capital. The Montaka process, which seeks to: (i) acquire high-quality businesses for less than they are worth; and (ii) sell deteriorating businesses with unreasonably high market-implied expectations, is a process that reduces the probability of permanent capital impairment. It is low risk – but it is not always going to produce low volatility.

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While in New York during the June quarter, your author was catching up with a close friend who also happens to be a finance and economics professor at Columbia University. Upon describing Montaka's strategy within the volatile global market environment, he succinctly summarized the challenge: "You are selling long-run expected returns, when all investors can see is short-term price movements." It is, indeed, difficult to sell something that is unobservable.

This is precisely the challenge for investors. Month-to-month returns carry with them a lot of noise and carry little information about long-run expected returns. Expected returns come from the investment process and the discipline with which this process is carried out. We encourage investors to remain focused on the investment process and the resulting medium and longer-term outcomes when investing in equities. Focusing on month-to-month returns can be distracting and emotionally testing.

And global volatility is only set to continue, in our view. We are living in a very strange and unprecedented financial world. At the writing of this letter, the following statements are true:

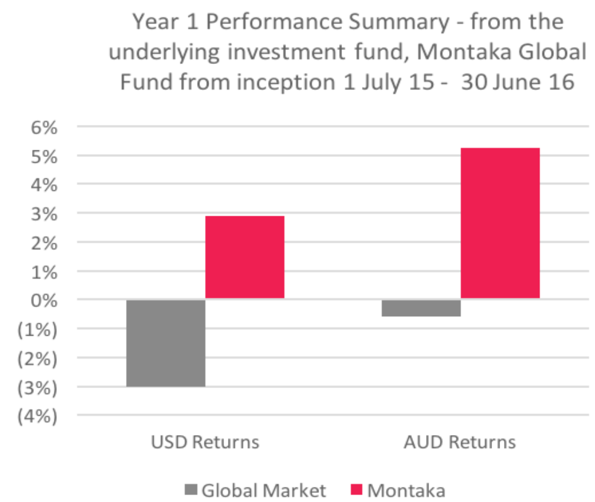
- You need to pay the German government for the privilege of lending to it for more than 15 years. (Yes, normally one would expect the borrower to pay the lender, but not in this case).
- Indeed, you need to pay the Swiss government to lend to it for 50 years!
- China's private investment growth is running at less than four percent – approximately one third the rate of growth that was being achieved this time last year.
- For the first time in history, the European Central Bank (ECB) has begun buying corporate bonds in the open market and directly from companies. (Remember, the money used to purchase these assets is created out of thin air).
- Britain has voted to leave the EU and has fallen into a state of political disarray.
- Despite many positive recent indicators pointing to strength in the US labor market, the May data for US Nonfarm Payrolls was the lowest monthly print since 2010.
- The US 10 year bond yield recently fell to its lowest level ever!
- Donald Trump is one vote away from being the President of the United States.

The above statements are not intended to scare investors; they merely highlight the new reality in which we find ourselves. Many of these statements would have been considered completely unrealistic only a few years ago. This begs the question, therefore: what unthinkable statements will be true over the coming few years? By definition, we do not know what we do not know. All we can do is make decisions with the premise that the world is uncertain and full of unpredictable events.

This is why we believe in the Montaka strategy. It seeks to protect the downside via its short portfolio; it seeks to generate stock-specific "alpha" through detailed, fundamental analysis of individual businesses; and the strategy is flexible. By flexible we mean the ability to invest across geographies, across industries and across company sizes. The Montaka strategy is also flexible in how much net market exposure (long exposure, less short exposure) can be taken at any point in time. Said another way, we view Montaka's short portfolio as an insurance policy which can be ratcheted up or down in size depending on whether or not we think we need more or less insurance given the global market conditions.

* * *

The data below relates to the Montaka structure, from its inception on 1 July 2015 to 30 June 2016 - in both US dollars and Australian dollars. In US dollar terms (the functional currency of the Montaka Global Master Fund), we finish our first year with returns of approximately 3%, net of fees. While this does not sound like much, it compares favourably to the MSCI World Total Return Index which declined by 3% in the same currency. We accept that due to timing difference, the Montaka Global Access Fund has been less successful. We are confident we can do better in the future.



I would like to thank my incredibly talented and dedicated colleagues for their hard work and discipline over the first twelve months of Montaka's life: Chris, George and Paul. Our team is truly world class and it is my privilege to be working with them. In addition, we welcomed Daniel Wu to the Montaka research team in June. Daniel is an extremely intelligent analyst that joins us from Goldman Sachs and UBS. We very much look forward to working with Daniel to collectively deliver great capital preservation and investment returns to our investors.

Sincerely,

Andrew Macken

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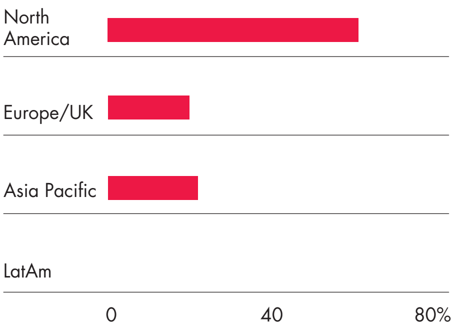
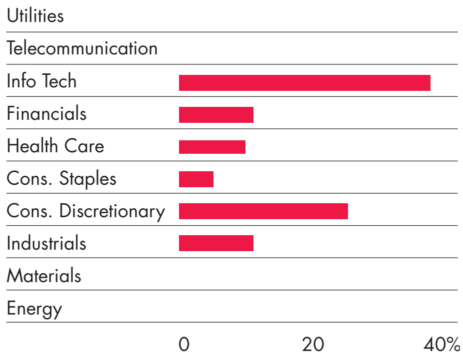
JUNE 2016

LONG PORTFOLIO*

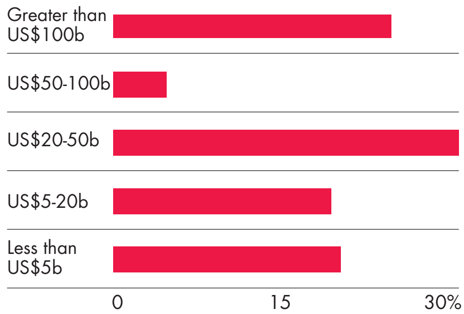
GEOGRAPHIC EXPOSURE (Country of domicile)



INDUSTRY EXPOSURE

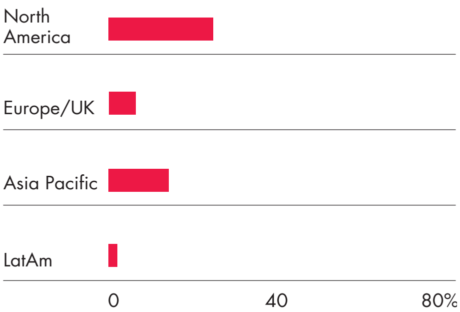


MARKET CAP EXPOSURE

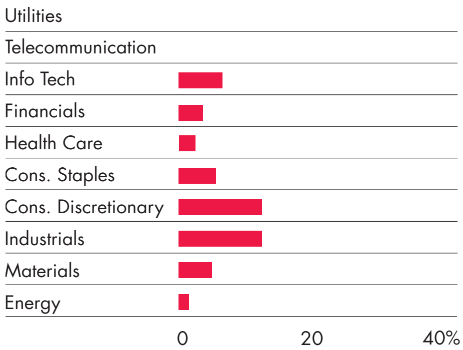


SHORT PORTFOLIO*

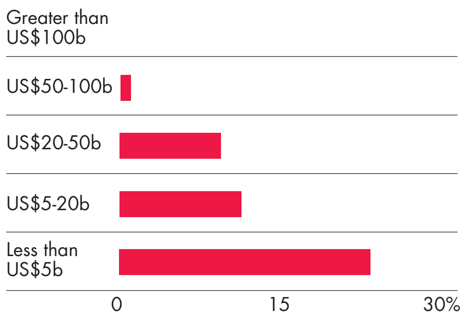
GEOGRAPHIC EXPOSURE (Country of domicile)



INDUSTRY EXPOSURE



MARKET CAP EXPOSURE



Note: exposures shown as % of NAV

** all exposures, metrics & positions are derived from the underlying investment fund*

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