

Monthly NTA Statement

December 2014

Ellerston Global
Investments Limited

ACN 169 464 706

14 January 2015

Ellerston Global Investments (**ASX: EGI**) advises the unaudited Net Tangible Asset backing (**NTA**) per share of the company as at 31 December 2014.

NTA per share	Before Tax	After Tax
31 December 2014	\$1.0198	\$1.0139

The NTA does not include or adjust for Loyalty Options.

Loyalty Options will vest on the Vesting Date of 10 April 2015 if and only if, the applicant holds the same or a greater number of Shares as applied for in the IPO.

Ian Kelly
Company Secretary

Introduction

We are pleased to provide to investors our first quarterly investment report, despite just 2 months of trading activity. We will be providing an update every quarter henceforth, which will include major new investments and a brief summary of selected new positions in the Portfolio.

As this is the start of a New Year, a Market Outlook for 2015 is also included.

Portfolio Structure

As previously communicated to investors, Ellerston Global Investments (**EGI**) aimed to be at least 50% invested within 3 months of listing. This has been reached ahead of schedule, by year end 2014. Consequently, the portfolio is now in a “steady state” with any increase in exposure optional, rather than obligatory. We anticipate lifting our exposure to ~75% over the next 3 months.

IT IS IMPORTANT THAT INVESTORS NOTE THAT THE FUND HAS ACHIEVED ITS MINIMUM INVESTMENT MANDATE REQUIREMENT FROM JANUARY 1 2015.

We noted in previous correspondence that EGI was launched in the context of our view of global markets, namely:

1. The recovery from the GFC is over and a process driven, stock picker’s approach to investing may be superior to a “beta-driven” fully invested approach.
2. The International developed markets provide a superior risk reward ratio to Australia for the foreseeable future.
3. Quantitative Easing or the lack of QE may be a driver of stock market returns in 2015 and 2016. Consequently, the decision to hedge or not hedge the underlying currency exposure to the specific international equity is a decision that is equally as important as the specific stock picks.

With that in mind, the US dollar exposure of the portfolio is unhedged and the Euro and Sterling exposures are currently hedged.

Although currency moves may be extreme in 2015, we are stock pickers not currency traders and our objective therefore is to see that the portfolio rides currency tailwinds and avoids currency headwinds.

Market Outlook

Although our outlook on the market has limited bearing on our stock picks, it does drive our overall exposure to the market.

We remain constructive. The US remains on track to “lift off” which can only be confirmed by the Federal Reserve raising rates. The collapse in energy prices is bad for the energy sector but very, very positive for the non-energy sectors of the US stock market.

Simplistically, the mark to market for energy equities is savage and their valuation has “moved down in the elevator.”

The boost that comes from lower input costs, greater savings and higher consumer spending will be gradual and continue all year if oil prices remain depressed. Just as “energy price dependent” equities “came down” in the elevator, the beneficiaries will go up “by the staircase” all year.

However, this may well be a bumpy ride in 2015. Essentially, the world produces approximately 90m barrels of oil a day. At the “old price” of US\$100 per barrel and 100 days of inventory in the system, the value of total inventory was $90\text{m} \times 100 \times 100$ which equals US \$900bn.

At the “new price” of US\$50 per barrel, the value of this inventory is US\$450bn lower. There is a “mark to market” loss of US\$450bn which must flow through the system. At some point soon, the victims will show up. With circa 25% of US high yield market being energy related, there is a bump in credit markets still ahead.

European QE draws closer, delayed only by the Greek elections and the political positioning of the Syriza party. The resolution of the Greek election will begin QE. A win by the incumbents could bring debt relief from the EU. A win by Syriza could force a renegotiation anyhow with the ECB and EU eventually doing whatever it takes to hold the recovery together. However, the ECB seems to be looking for a French fiscal response before it ramps it up.

The lesson we investors have learnt from US QE is that the performance of the underlying economy (in this case, the EU) drives QE, which drives the performance of financial assets. The best performance from the US equity markets came in 2009 and 2013 despite a soft economy, with the Federal Reserve running the printing presses at full clip.

Perversely, the weak European economy bodes well for European equities (particularly German and Spanish) over the next two years. Similarly, the aggressive easing stance of the BOJ creates a powerful backdrop for Japanese equities with the background of a sharply weaker yen. US/¥ has broken a 30yr uptrend which may presage some fireworks in all Japanese asset classes.

The portfolio has not yet invested any capital into Japan at this point but expects to do so in the coming quarter.

China on the other hand continues to slow. As the economy continues its transition from one of industrial production to consumer consumption, it will become impossible to revisit the growth rates of the past decade. 6% GDP growth appears to be the line in the sand, and as growth comes down the leadership will stimulate. The point to emphasise here is that the stimulus packages in China will be designed to hold growth above stalling speed rather than ushering in a return to the past.

Governments and Central Bankers around the world have become used to aggressive intervention, using both fiscal and monetary tools to tackle sluggish economies. While this continues, we can be confident of continuing financial asset inflation.

To summarise our market outlook,

- Long-term rates in developed markets have collapsed ✓
- QE is running in Japan ✓
- QE is coming in Europe ✓
- Equity valuations are full but equities do look compelling versus bonds ✓
- Inflation is falling ✓
- The new oil price is very positive for “non-energy” earnings ✓

With the proviso of geo-political risk, which is significantly more elevated than in previous years, the outlook for equities is reasonably positive.

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Portfolio

As at the 31 December 2014, investments have been made in 17 companies.

TOP 5 Portfolio Holdings	
Company	Country
Vivendi	France
Synchrony Financial	US
Experian	UK
Nielsen	US
Google	US

This quarter we have chosen to highlight our investment in Synchrony Financial which is the former wholly owned US consumer credit business of GE Capital.

Other stocks also included this quarter for comment are FICO, Hispania Activos Inmobiliarios, TrueCar and Tesco.

Synchrony Financial

Spin Off – Dominant franchise in growing consumer credit market with capital management initiatives to come.

Synchrony (**SYF**) is the former wholly owned US consumer credit business of GE Capital. GE sold a 16% stake via an IPO in July 2014 and plans to spin off the rest of the company to GE shareholders in late 2015.

SYF has \$56.8 billion (Q314) of loan receivables which it funds through a mixture of wholesale funding and deposits. A key strategic asset of the company is its banking license and low cost deposit funding with deposits having grown over the past year from \$22.2 billion to over \$32.7 billion.

The long term sector dynamics of SYF's business are attractive as are its dominant market position and retail relationships. At 11.5x PE FY15 and 2x book value, we believe we are paying a fair price for the leading private label credit card business in the US with significant upside from potential capital management initiatives and material tailwinds that will drive shareholder returns.

Company Overview

The company has three divisions and generates all of its revenues domestically in USD.

Retail Card: 74% of Total Interest Income, 68% of Receivables

Metrics: Loan Receivables \$38.5b, Retail Partners 19, Partner Locations 33,000

Partners include: Lowe's, Sam's Club, GAP, Walmart, JCPenney, Amazon.com and TJX

Leading provider of private label credit cards through partner programs with a 42% share in a highly concentrated market. Private label credit cards are Partner-branded credit cards that are used for the purchase of goods and services from the Partner. The average length of a relationship with a Retail Card Partner is 15 years. The Retail Card programs typically are exclusive with respect to the credit products offered at that Partner.

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Payment Solutions: 13% of Total Interest Income, 20% of Receivables

Metrics: Loan Receivables \$11.5b, Partners 62,000, Partner Locations 117,000

Partners include: hhgregg appliances & electronics, LAZYBOY, Ashley Furniture and TireDiscounters.

Leading provider of promotional financing for major consumer purchases, offering primarily private label credit cards and instalment loans.

CareCredit: 13% of Total Interest Income, 12% of Receivables

Metrics: Loan Receivables \$6.8b, Partners 155,000, Partner Locations 185,000

Partners include: VAC Animal Hospitals, LasikPlus, sonobello, and Beltone.

Leading provider of promotional financing to consumers for elective healthcare procedures or services, such as dental, veterinary, cosmetic, vision and audiology. SYF offer customers a CareCredit-branded private label credit card that may be used across its network of CareCredit providers.

The company has a number of tailwinds that should drive growth:

1. *Recovering US Economy:* SYF is leveraged to improved US consumer and employment conditions as well as falling oil prices. Delinquencies should be stable and loan growth could accelerate.
2. *Customer Acquisition & Increased Penetration:* SYF renewed its 5 largest programs in 2013 & 2014. Some retailers have no offering while others run in-house private credit card platforms, including Nordstrom and Target. This represents potential opportunities for additional growth.
3. *Technology:* With 60 million active accounts and 109 million open accounts SYF has access to a vast amount of consumer data (such as customers' purchase patterns and payment histories) from the hundreds of millions of transactions its customers make each year. SYF is developing new tools to assess this data to develop and deliver valuable insights that can be used to improve the effectiveness of marketing strategies leading to incremental growth for both Partners and SYF's business. In addition, SYF is pursuing the mobile opportunity with various platforms including Apple Pay. Purchase volume from SYF's online and mobile channels increased 62% from 2010 to 2013.
4. *Separation from GE and Capital Management:* SYF's current capital position of 15.1% Tier 1 Common Ratio is very strong and higher than peers. This ratio is expected to increase meaningfully with the company unable to make any capital management decisions until the separation from GE and final regulatory approval. SYF will then be in a position to undertake capital management initiatives in the form of a dividends and/or buybacks.

We believe that GE may have spun off this business in order to achieve a tax-free take out to its shareholders.

Hispania Activos Inmobiliarios

Post IPO – Spanish property prices were hit hard during the financial crisis and this asset class is primed for a recovery.

Company Overview

Hispania Activos Inmobiliarios (**Hispania**) listed on the Spanish Stock Exchange in March 2014. It was established to acquire and manage real estate assets in Spain to take advantage of the downturn in Spanish real estate. The company raised €550m at €10 per share. The investment vehicle is externally managed by Azora, an independent private equity manager specialized in real estate investments. Hispania has a number of cornerstone investors including Paulson and Soros, each with a 16.7% holding. Management have an ownership in excess of 2%.

The Spanish economy was one of the hardest hit during the recent financial crisis. For some perspective, there were only 35,000 houses built in Spain in 2013 compared to over 500,000 in 2007.

Hispania has begun to assemble a high quality real estate portfolio investing primarily in residential properties, offices and hotels in Spain. The company has acquired 23 properties since its listing up to September 30th, for a total investment of €372 million, across three main asset categories: Residential: 20%, Hotels: 20%, Offices: 60%.

A compelling addition to the investment opportunity was the company announcement in November 2014 regarding its takeover offer and recapitalisation proposal for the distressed listed Spanish property company Realia. Hispania is working with debt holders on an exclusive basis with a successful recapitalisation reliant on at least 55% of the shares being tendered into the takeover offer. The deal is complex with a number of key components that need to be executed. Should it complete in its proposed form we believe there would be significant value creation over the long term for Hispania shareholders. Even if the Realia deal fell away, we think the risk/reward with the current asset base and capital position of Hispania is a compelling way to benefit from a recovering Spanish property market.

While the proposed Realia transaction is complicated, we believe that Hispania will be a very attractive company well positioned to ride the tailwind of European quantitative easing.

Fair Isaac Corp (FICO)

Embedded Optionality – Renewed focus on consumer product division provides tremendous upside optionality.

Traditionally, FICO's focus has been on the enterprise customer, but a recent deal with Experian highlights a renewed push to grow its consumer product business. The potential upside from this is material.

Company Overview

Founded in 1956, FICO introduced analytic solutions such as credit scoring that have been responsible for making credit more widely available in the US.

The industry-wide adopted FICO® Score is the standard measure of consumer credit risk in the United States. To put the value of the FICO® Score in perspective, 90 percent of all U.S. consumer lending decisions use the FICO® Score, 25 of the largest credit card issuers and 25 of the largest auto lenders rely on the FICO® Score for consumer credit risk analysis and federal regulatory compliance.

The company has expanded into software and tools to manage risk and fight fraud (2.5 billion credit cards globally are protected by FICO Fraud Systems) as well as decision management with 95% of the largest financial institutions in the U.S. being FICO clients.

TrueCar

Post IPO – Delivering significant technological benefits to an “old world” industry.

TrueCar operates in one of the largest segments of the US economy (2015F sales of new cars and trucks - 17 million units) with a growing market share of all new cars sold in the US (3.7% Q314, 2.6% Q313). The company expects full year 2014 revenue of \$206m with \$9.2m in adjusted EBITDA and longer-term adjusted EBITDA margins of 35%+. Further opportunities for TrueCar to expand its offering include TrueTrade which the company plans to launch in early 2015 that will provide users with an estimated daily market value for their existing cars and a guaranteed trade-in price as well as other developments such as TrueLoan and TrueLease which will provide users with more convenient ways to finance their cars at TrueCar Certified Dealers.

Company Overview

TrueCar listed on the 16th May 2014 and currently has a \$1.5b enterprise value.

The company is a negotiation-free car buying and selling platform that aims to bring transparency to car purchasing. The company's data driven online platform and technology infrastructure enables users to obtain market-based pricing data on new and used cars and to subsequently connect to its network of TrueCar Certified Dealers.

TrueCar benefits the consumer by providing upfront pricing information from its network which generally includes savings off the Manufacturer's Suggested Retail Price (MSRP) which the consumer may then take to the dealer in the form of a Guaranteed Savings Certificate and apply to the purchase of the car.

TrueCar has a national network of 8,149 franchised dealers (TrueCar Certified Dealers) on its platform up from 6,327 a year ago. This represents 26% of all new car franchised dealers in the US. Unlike lead generation platforms, TrueCar employs a pay-for-performance business model charging a fee (\$299 upon sale of new car) only when a consumer purchases a car using a TrueCar Certificate.

TrueCar is an odd company in the context of our portfolio as it could be argued that it is outside our fundamental bias. Value however is in the eye of the beholder. The business has over 25% of all US car dealers on its platform.

- In the last 3 years it has sold 1.5, 2.5 and 3.5% of all new cars sold in the US.
- Its revenue is growing at over 30% p.a.
- It has significant new earnings streams on the horizon with trade-ins and used cars.
- Companies in other industries with similar disruptive platforms are trading at 10x to 20x revenue (compared to TrueCar at 8x).

Tesco

Management Change – Impressive new management team has started to implement key strategic initiatives.

In our first note, we provided a brief summary on our investment in Tesco Plc. While it is still early days in the turnaround we believe that the right moves are being made by new CEO Dave Lewis.

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This multi-year turnaround will be volatile as the CEO seeks to set Tesco on the path of a sustainable recovery. When investing in a “fallen angel” such as Tesco we will move slowly and look to gain comfort as we “tick the boxes” at various stages of the turnaround. While improvements in the core business are visible, we are more impressed by the CEO’s review and strategy and it is clear that he has been given an open mandate by the board and that the tough decisions will be made for the benefit of the long-term viability of Tesco.

Company Overview

Tesco released its trading statement on 8 January 2015 and noted broad-based improvement in the UK business and in Europe. The CEO outlined his strategy to regain competitiveness in Tesco’s core UK business and strengthen the balance sheet. He is squarely focused on investing in the UK (in service, availability and price), reshaping relationships with suppliers and restructuring the cost base of the company.

Some key features of the company’s announcement:

- Appointment of Matt Davies, CEO of listed Halfords Group Plc as the new CEO for the UK and Ireland,
- Restructuring of the cost base to deliver savings of £250m per year – central overheads, simplification of store management structures,
- The consolidation of head office locations,
- The closure of 43 unprofitable stores,
- Significant revision to Tesco’s store roll out programme – 49 sites that will not be built, 23 still to be opened,
- Initiation of consultations to close the company defined benefit pension scheme,
- Significantly reduced capital expenditure budget next year of £1b (reduced from £2.1b this year),
- Disposal of Tesco Broadband and Blinkbox,
- Appointment of Goldman Sachs to explore strategic options for the Dunnhumby analytics business. Media reports suggest valuation of c£2b; and
- Elimination of final dividend for this year.

Tesco is a classic fallen angel. If a turnaround can be successfully implemented, the stock could be re-rated dramatically.

Should investors have any further questions or queries regarding the company, please contact our Investor Relations team on 02 9021 7797 .

All holding enquiries should be directed to our share registrar, Link Market Services on 1300 551 627 or EGI@linkmarketservices.com.au.

Important note

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