

Australian Enhanced Income Fund

October 2014 Investment Update and NAV

October 2014 NAV and Fund performance

The Fund's NAV at the close of business on October 31, 2014 was **\$6.433** per unit. This compares with the ex-distribution NAV of a unit at the close of business on September 30 of \$6.374. The change in NAV over the month of October represents a return of **0.93%**. The franking benefit for October was estimated to be **0.02%**.

ASX trading details

The Fund traded on market at the ASX at a slight discount to the most recently published NAV of a unit over the month of October 2014. The volume weighted average price (VWAP) for October 2014 was **\$6.36**.

	1 month	3 months	12 months*
Australian Enhanced Income Fund	0.93%	-1.30%	5.83%
UBSA Bank Bill Index	0.23%	0.67%	2.66%

*Returns do not include the benefit of franking. Past performance is not necessarily a guide to future performance.

Events of October

- The ASX listed hybrid sector returned 0.71% for the month. This compares with the All Ordinaries Accumulation Index return of 3.96% and the UBSA Bank Bill Index return of 0.23%.
- 4 new hybrid securities listed this month – all opened at below PAR.

Fund performance

The Fund outperformed the broader market slightly this month. The Fund's net return (excluding the benefit of franking but after fees) for the year to end 31 October 2014 increased to 5.83% from 5.66% previously.

Risk and return

If you asked any investor about risk and return, they'd tell you that to get a higher return you need to take more risk or alternatively investing in riskier assets will get you a higher return. It's what they have been taught *ad infinitum* about investing. However, it is not true all of the time. The chart overleaf is a comparison of the Elstree Hybrid Index (green line) and the All Ordinaries Accumulation Index (blue line) from 31 December 1999 to 31 October 2014 (the starting point of December 1999 is the first point we began to collect aggregated hybrid performance data). The base is 1000 at 31 October 2014. What the chart shows is the amount you need to invest in either hybrids or equities to receive \$1000 at October 31, 2014. Any time one index series is below the other indicates cheapness of that series and when the indices intersect the returns of each series are identical from that point in time to 31 October 2014.

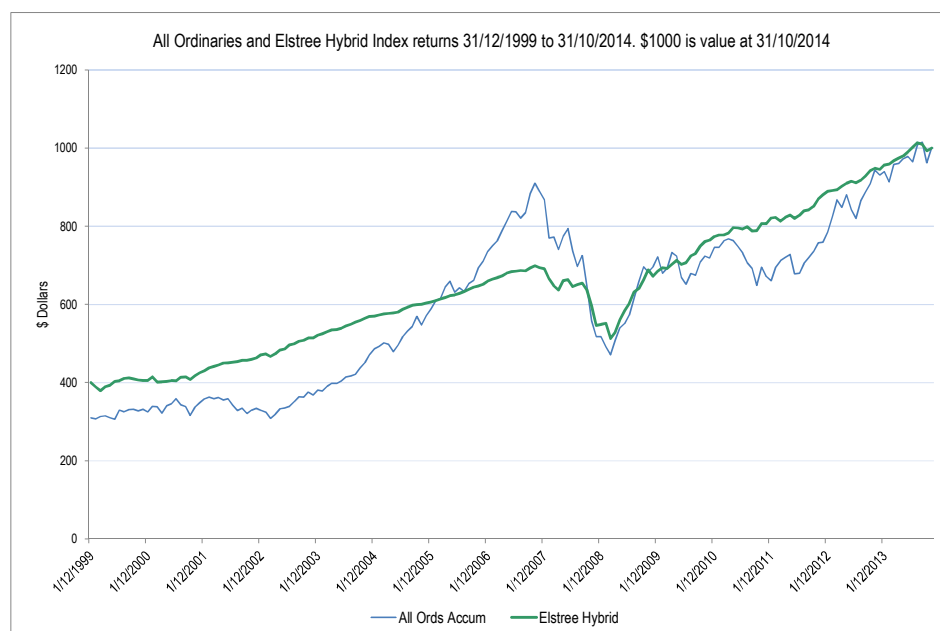
Takeaways are;

- While there are many takeaways the most glaring is that while the return outcomes are similar hybrids have achieved the return outcome they have achieved with about 40% of the volatility of equities. Other important takeaways are;
- (i) The total additional return from equities over hybrids is around 1% p.a. over the 14 year return period.
 - (ii) Equity returns have been assisted unequivocally by falling interest rates.

Arguably, that tail wind is now ending whereas hybrid margins are around 3 times wider now (i.e post GFC) than they were in the first half of the period (i.e pre GFC).

(iii) The return period is not 'cherry picked' with hybrids, which are credit instruments, experiencing the worst credit event since the Great Depression.

(iv) Returns of hybrids and equities since the GFC have been almost identical (once again hybrid volatility has been significantly less over the period).



Issued capital and NAV as at close of business 31 October 2014

	31 October 2014	Previous month	Monthly change	Change over Quarter
Total number of ordinary units	2,267,498	2,264,627	2,871	-124
Net Asset Value (NAV)	\$6.433	\$6.374#	0.93%	-1.30%

- Returns exclude the franking benefit. Past performance is not necessarily a guide to future performance. # Ex-Distribution.

Performance History

	June 2014	July 2014	Aug 2014	Sept 2014	Oct 2014
Change in NAV	+1.31%	+1.41%	-0.50%	-1.72%	+0.93%
Change in UBSA Bank Bill Index	+0.22%	+0.23%	+0.23%	0.21%	+0.23%
Comparison to Bank Bill Index	+1.09%	+1.18%	-0.73%	-1.93%	+0.70%
Franking benefit (estimated)	+0.08%	Zero	+0.13%	+0.18%	+0.02%
Total Return including franking	+1.39%	+1.41%	-0.37%	-1.54%	+0.95%

For additional information please contact **Norman Derham** at Elstree Investment Management Limited on (03) 8689 1348 or by email info@eiml.com.au. While the information in this report has been prepared with reasonable care Elstree Investment Management Limited accepts no responsibility for any errors, omissions or misstatements however caused. This is general securities information only and is not intended to be a securities recommendation. This information does not account for your individual objectives, needs or financial situation.