JENCAY
capital

AFS Licence Number 402024
ACN 148810413

# Jencay Australia Investment Fund

## Quarterly report - March 2012

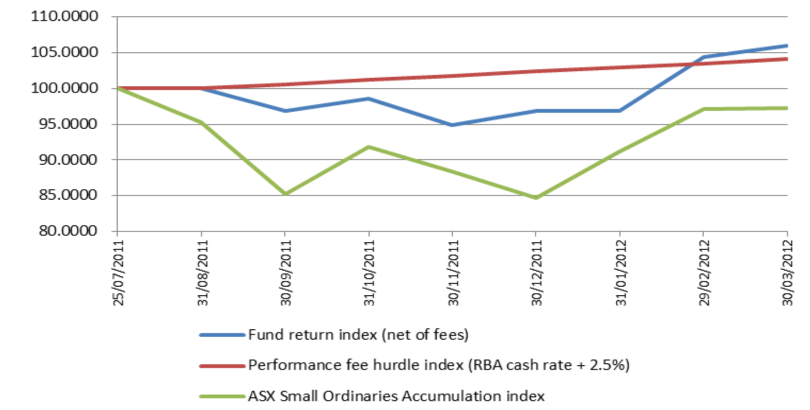
## Performance

| Returns are net of fees, exclude buy/sell spreads, assume reinvestment of distributions/income and are not annualised | Since inception (25 July 2011) | Quarter to 31 March 2012 |
|---|---|---|
| Fund total return | 6.03% | 9.41% |
| Performance fee hurdle (RBA cash rate + 2.5%) | 4.12% | 1.70% |
| ASX Small Ordinaries Accumulation Index return | (2.66%) | 14.98% |

## Unit Price at 31 March 2012

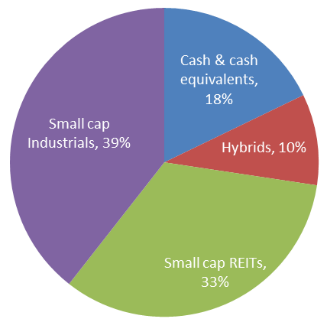
| | | |
|---|---|---|
| **NAV per unit** | | **AUD 1.0603** |
| Application price | (0.5% spread added) | AUD 1.0656 |
| Redemption price | (0.5% spread deducted) | AUD 1.0550 |

## Performance Chart




The chart shows the movement in value of AUD100 invested in the Fund at inception, relative to the Reserve Bank of Australia cash rate plus 2.5% (performance fee hurdle) and relative to the ASX Small Ordinaries Accumulation index. Returns are net of fees, exclude buy/sell spreads and assume reinvestment of distributions/income. Although inception date was 25 July 2011, fees only started accruing from 1 September 2011.

## Fund Composition




Fund size : AUD 5.9m

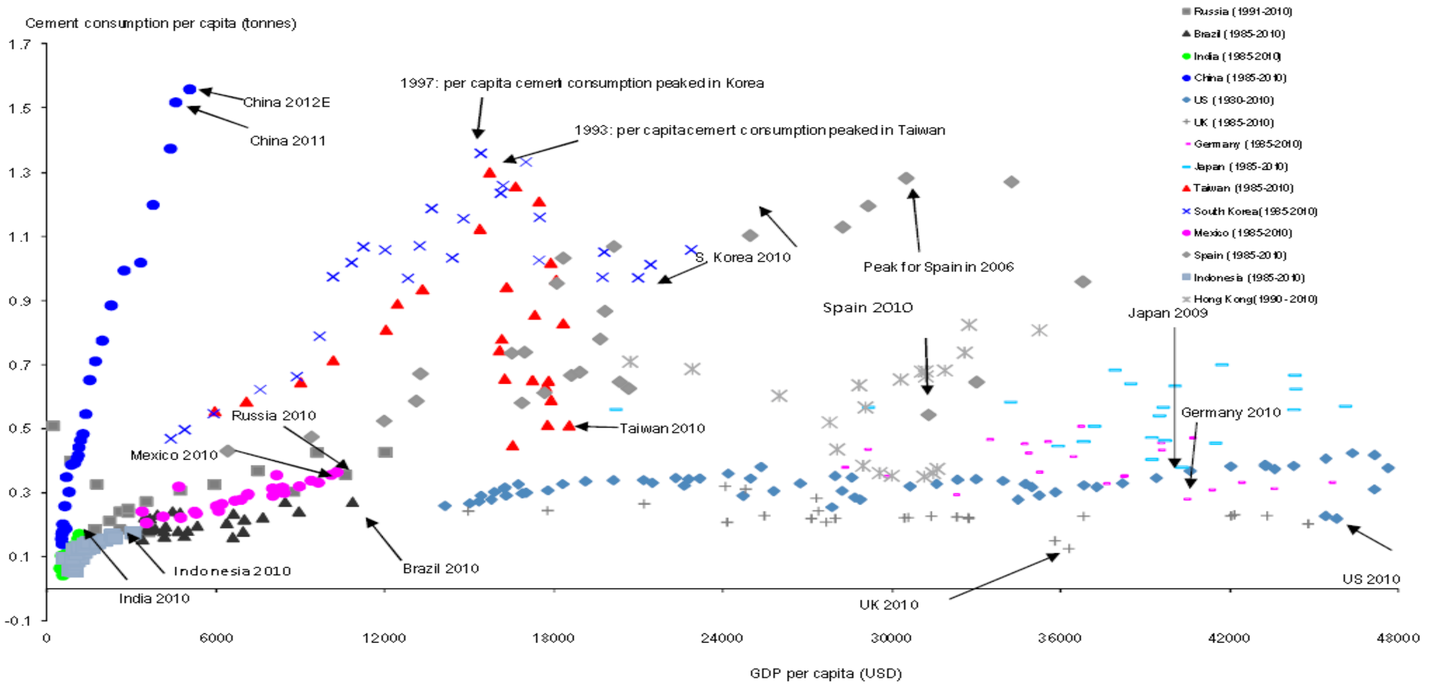
The strong absolute returns for the quarter pushed the fund's return index above its performance fee hurdle for the first time. The bounce was driven largely by the improvement in market sentiment and in particular the very strong performance of the Australian small cap index in the quarter. Large movements in share prices of individual stocks necessitated rebalancing of the portfolio and since December the following three stocks fell out of the top 10 after strong performances: Aspen Property Group, Centro Retail and Australand hybrid. Those positions were replaced by the following stocks which we believe now offer greater risk adjusted upside: Austal, Reckson New York and Elders. Brief descriptions are included below.

## Top 10 Positions at 31 March 2012

| Weight % | Name | Summary Investment Case |
|---|---|---|
| 18 | Cash & cash equivalents | 11% is cash on call deposit with the custodian, JP Morgan. The 7% balance is held in an ASX listed exchange traded fund whose only asset is a USD call deposit with JP Morgan. |
| 7 | Servcorp | World's second biggest serviced office business behind Regus, but is considered the market leader. Founder and CEO owns 50%. 1/3rd of its market cap is backed by cash with no debt. Enterprise value is approximately 3 times our estimate of EBIT in three years' time. Servcorp has strong long term growth potential and a large portion of earnings are generated outside Australia. |
| 7 | Astro Japan Property | Real Estate Investment Trust (REIT) holding retail and office properties in Japan. The share price is half of its Net Tangible Asset Value (NTA), on a forward earnings yield of 20%. 60% of earnings are being retained to amortise debt (gearing 60%) which should grow earnings and NTA going forward. Japanese office rentals seem to be close to bottom of cycle. |
| 6 | Paperlinx (Hybrid and Ordinary) | The world's second largest paper merchant. The exposure to the company is held via perpetual preference shares (hybrid) and ordinary shares. The hybrid price is less than 20% of face value and the ordinary share is trading at less than half of NTA (consisting mainly of paper inventory and receivables). |
| 6 | Austal | The world's leading aluminium boat builder. It has secured two US Navy contracts to produce 20 ships that will keep Austal's US facility in full production to 2018. The expected free cash flows from those 2 contracts alone exceed Austal's current enterprise value. This means that any additional earnings generated from servicing the delivered Navy ships; their currently underutilised Australian and Philippine production facilities; and any earnings generated post 2018 are free at the current share price. |
| 6 | Reckson New York Property | Real Estate Investment Trust (REIT) holding suburban office property in the New York tri-state area. The share price is 1/3rd of its NTA and on a forward earnings yield of 20%. The trust has successfully refinanced most of its debt and the markets in which the properties are located seem to have bottomed. |
| 5 | Fisher and Paykel Appliances | Appliance manufacturer with dominant market share in New Zealand and No.2 in Australia as well as a presence in North America, Europe and Asia. It also has one of the top consumer finance businesses in New Zealand. The company has been responsible for many of the world's appliance innovations over the last decade however the stock price is less than its NTA, on a P/E of 9x despite earnings being at cyclical lows and the company having strong growth prospects. |
| 4 | Salmat | Australia's leading provider of one-to-one communications including online and physical catalogue distribution, contact centres, essential mail and digital communication. Founders hold 40%. Despite a history of excellent cash generation, earnings growth and investment in new innovation, the stock is trading on 7x historical earnings with a fully franked dividend yield of 10%. |
| 4 | Mirvac Industrial Trust | REIT holding warehouse property in Chicago. Debt has been refinanced on a long term basis. The share price is less than half of NTA and on an underlying earnings yield of circa 20%. The cycle seems to have bottomed with our expectation that valuations, rentals and occupancy will improve going forward. Any A$ weakness will also be beneficial. |
| 4 | Elders (Hybrid and Ordinary) | 2nd biggest farm supply and service network in Australia and one of Australia's oldest businesses. The fund holds both its perpetual preference shares (hybrid) and ordinary shares. After near death due to excessive debt and a failed conglomerate strategy, Elders, under new management, has sold businesses, substantially reduced debt and seems to be on a sustainable path. Nevertheless, the hybrid price is 1/3rd of face value with our expectation that hybrid distributions will resume in 2014 (30% forward yield). The ordinary share is trading at less than half of NTA on a forward P/E of less than 5x. |

## Manager's Observation

Although approximately 30% of the Australian stock market index comprises resource companies, it may seem surprising that the fund has almost zero exposure to resources. After a decade long commodity up-cycle, we have struggled to find compelling bargains in this space. We also believe the factors that drove the surge in commodities over the last decade are not sustainable, especially in light of the massive increase in supply that will hit the markets over the next few years. We believe that the chart below, illustrating the unprecedented use of cement in China on a per capita basis (measure of extent of construction, also benefitting iron-ore, copper and coal demand), relative to other countries at similar stages of development, provides compelling support for our views:




*Source: JP Morgan*

## Fund Key Features

*Comprehensive Terms are contained in the Information Memorandum which can be downloaded from the website www.jencay.com.au or sent to you upon request*

| | |
|---|---|
| **Custodian** | JP Morgan Chase Bank N.A. |
| **Administrator** | White Outsourcing Pty Ltd |
| **Fund auditor** | PricewaterhouseCoopers |
| **Inception** | 25 July 2011 |
| **Investment strategy** | The Fund seeks to buy securities trading significantly below fair value (bargains). Cash will be held on deposit when bargains are not available in the market. The fund will have a small cap bias in accordance with the Manager's opinion that the majority of bargains are found amongst small caps. |
| **Product type** | Wholesale managed investment scheme available to wholesale clients and sophisticated investors |
| **Investment universe** | All securities listed on the Australian Securities Exchange (ASX) and cash to be held on deposit |
| **Fund size cap** | $200 million in net subscriptions |
| **Investment restrictions** | ▪ Maximum of 40 individual security holdings<br>▪ Maximum exposure of 15% to a single security<br>▪ No short positions<br>▪ No leverage<br>▪ A maximum of 10% of the fund can be invested in companies with no earnings history such as biotechnology, resource exploration, new technology |
| **Minimum initial investment** | $100,000 |
| **Minimum additional investment** | $20,000 |
| **Minimum redemption amount** | $20,000 |
| **Base management fee** | 1% p.a. excluding GST. Management Expense Ratio 1.025% p.a. inclusive of non-recoverable GST |
| **Performance fee** | 20% of returns above the Hurdle rate subject to a high water mark. The Hurdle rate is the Reserve Bank of Australia Cash Rate Target plus 2.5%. |
| **Entry fee** | None |
| **Buy spread** | 0.5% |
| **Sell spread** | (0.5%) |
| **Redemption notice** | 6 months' redemption notice required otherwise 5% early exit penalty |

## Contact Details


| | | | |
|---|---|---|---|
| **Trustee and Investment Manager** | Web<br>Tel<br><br>Email | www.jencay.com.au<br>+61 2 9238 6177<br>+61 415 233 512<br>info@jencay.com.au | Jencay Capital Pty Ltd<br>Level 57 MLC Centre<br>19-29 Martin Place<br>Sydney<br>NSW 2000 |
| **Administrator** | Tel<br>Fax<br>Email | +61 2 8236 7701<br>+61 2 9221 1194<br>registry@whiteoutsourcing.com.au | White Outsourcing Pty Ltd<br>Level 7, 20 Hunter Street<br>Sydney<br>NSW 2000 |


## Disclaimer