Monash ABSOLUTE INVESTMENT COMPANY

Monash Absolute Investment Company Limited

Monash Absolute Investment Company Limited (ASX: MA1) **Friday 2 September 2016**

August 2016 End of Month Update

In the interests of keeping the market fully informed of performance on a timely basis, we release a preliminary estimate of the Pre-Tax Net Tangible Asset Backing per share. It is only a guide, the official NTA will be released later in the month. We estimate that as at 31 August 2016 the NTA Pre-Tax was $0.9700.

Company Strategy

The Monash Absolute Investment Company offers investors access to an investment strategy that seeks to:

- achieve a targeted positive return over a full investment cycle; and
- avoid a negative return each financial year

The Company is benchmark unaware, style and stock size agnostic, both long and short, and only invests in compelling opportunities. In keeping with the Company's absolute return objectives, if the investment manager cannot find stocks that meet the very high return hurdle requirements, the Company will preserve that capital in cash at bank.

Commentary

The NTA (est) was down 1.11% (after fees) for the month of August, during which the equities market was also weak. The ASX200 fell 1.55% for the month.

The key contributors were stocks held in medical device companies and retailers. The medical device companies are making good progress. Airxpanders (ASX: AXP) rose 20% after presenting at a broker's conference, and Impedimed (ASX: IPD) was up a further 15% following the FDA's positive announcement regarding Digital Health. The retailers were Kogan (ASX: KGN) which rose 15% with a beat to its Prospectus forecasts, Lovisa (ASX: LOV) was up 13% as it U.K. store roll out accelerates, and Harvey Norman (ASX:HVN) was higher by 11% with strong sales and margins.

There were two key detractors. G8 Education (ASX: GEM) was down 20% on weaker margins and the Company's short position in Insentia (ASX: ISD) was up 21% due to a strong outlook, before we covered. These together cost the Company's portfolio over 2%, with the remainder of the Company's holdings, on balance, doing well.

Company at a Glance 31 August 2016

ASX Code - Shares	MA1
ASX Code - $1 Options Sep17	MA1O
Portfolio Size	$51.1m
Share Price	$0.945
Option Price	$0.019
Shares on Issue	52.5m

Portfolio Structure 31 August 2016

Outlook Stocks (Long)	20 Positions	71%
Outlook Stocks (Short)	1 Position	-4%
Event, Pair and Group (Long)	5 Positions	15%
Event, Pair and Group (Short)	1 Position	-3%
Cash		21%
TOTAL		**100%**
Gross Exposure		92%
Net Exposure		79%

NTA (unaudited) 31 July 2016

NTA Pre Tax	$0.9810
NTA Post Tax	$0.9868

Estimated NTA (unaudited) 31 August 2016

Estimated NTA Pre Tax	$0.9700

Return Estimate to 31 August 2016

	1 month	Since Inception 12 April 2016
NTA Pre Tax	-1.1%	0.7%

For more information about the Company and the strategy please refer to the Monash Investors website at www.monashinvestors.com. You can also follow us on Liverwire here or subscribe to our updates here

Retailers Ramping Up

Retailers are a sector of the market whose earnings are difficult to forecast accurately. They are prone to surprise the market more than any other sector each reporting period. During the reporting month of August just passed, 10 went up more than 5% on the day of their result, and another 10 fell more than 5% on the day.

Retailers' profits are less predictable than other companies because small variations in their volumes and selling prices typically result in large variations to their profit margins, and it is hard for an outside observer to know what is going on with the quantity and mix of products sold and the prices at which they are selling them.

On the other hand, there are times when retailers can deliver strong growth in earnings over an extended period. This is evident when a firm rolls out a network of stores that are rapidly profitable (think the early days of Flight Centre or Harvey Norman) or whose customers are demanding more products that have high margin and high turnover (like JB Hi-Fi as it replaced floor space for records and musical equipment with consumer electronics).

Lovisa

Lovisa is a stock that the Company holds that has a long runway of store roll out opportunities ahead of it.

Lovisa retails low cost jewellery as fast fashion. The customers are principally young women who want the latest accessories to wear with their clothes. Lovisa has addressed this market by designing its own product, based on the latest trends from social media and fashion shows, and aims to replenish 15% of their inventory each week with new designs. So there is always something new to see in store. The stores have a relatively small footprint, yet high turnover.

This contrasts with fashion stores that are focusing on a wider demographic with a wider range of price points. Competitors also often have accessories as a smaller part of apparel stores, and do not specialise in it. The speed of Lovisa's inventory cycle is unique for specialist jewellery (Zara operates similarly in apparel) and its competitors have inventory cycles of 3 months plus.

The business model was rolled out rapidly in Australia, where they have 145 stores and it is mature. However, they are only at the beginning of their international store roll out, which accounts for 36% of group sales. Locations include New Zealand, South East Asia, the Middle East and South Africa. Critically all of these international operations have a similar return profile as Australia, demonstrating that this store format works across different international markets. They have 4 stores in the UK, and this is to be a particular focus of growth going forward following the success of their pilot program, which only started in November 2015.

The payback on a new store is between 4 and 8 months, with same store sales growth of around 4%pa. Given these exceptional returns on invested capital Monash Investors view is that there is little doubt that the Lovisa Management and Board will materially expand its store network. The size of the UK market is such that the store rollout in this market alone will easily double profits over time, and then there is Europe and the USA to consider. With Lovisa trading at a valuation discount to other retailers and with a dramatically greater growth runway, there is significant upside to the share price.

Kogan

Internet retailing has been one part of the market that has taken a bit of a beating lately. For example: Surfstitch, Temple & Webster and AHA Life. The Company did not invest in any of these. So it was good to see a company in which the Company did invest, Kogan, beat its prospectus forecast quite strongly.

Kogan started out as an on-line retailer of consumer appliances/electronics and has expanded into many other product lines, selling big brands as well as its own private label. It listed in order to raise capital to accelerate the growth of its private label range, which provides a higher margin than selling the brands of other manufacturers. The Kogan result beat its prospectus revenue and margin forecasts solidly, and they continue to enjoy an increase in on-line visits of over 20% pa. While they will not be giving guidance until their AGM, a mix change towards more private label and higher margin verticals should further support a strong outlook.

Harvey Norman

Harvey Norman was in the Company portfolio during August as an Event[i] Trade – the catalyst being its upcoming earnings result.

Harvey Norman is a business that has revenues and margins that are sensitive to building activity through selling bathrooms and kitchens, appliances, and furniture; and it is also a big seller of consumer electronics. When times are good, the percentage margin paid to its franchisees is narrowed, exaggerating the profit uplift to Harvey Norman (and when times are bad franchisees are subsidised).

Monash Investors saw that this reporting season was headed for a very good Harvey Norman result for two reasons. First there had been extremely strong building activity. Secondly, with the collapse of Dick Smith, competition had lessened in consumer electronics.

The result played out the way Monash Investors thought it would, and the stock rose and it largely beat expectations and then rose further again on the day of the result. The stock was then exited.

[i] Event means securities that Monash Investors has identified a near term event or catalyst that it believes should drive a share price reaction.