Hybrid market overview November 2015

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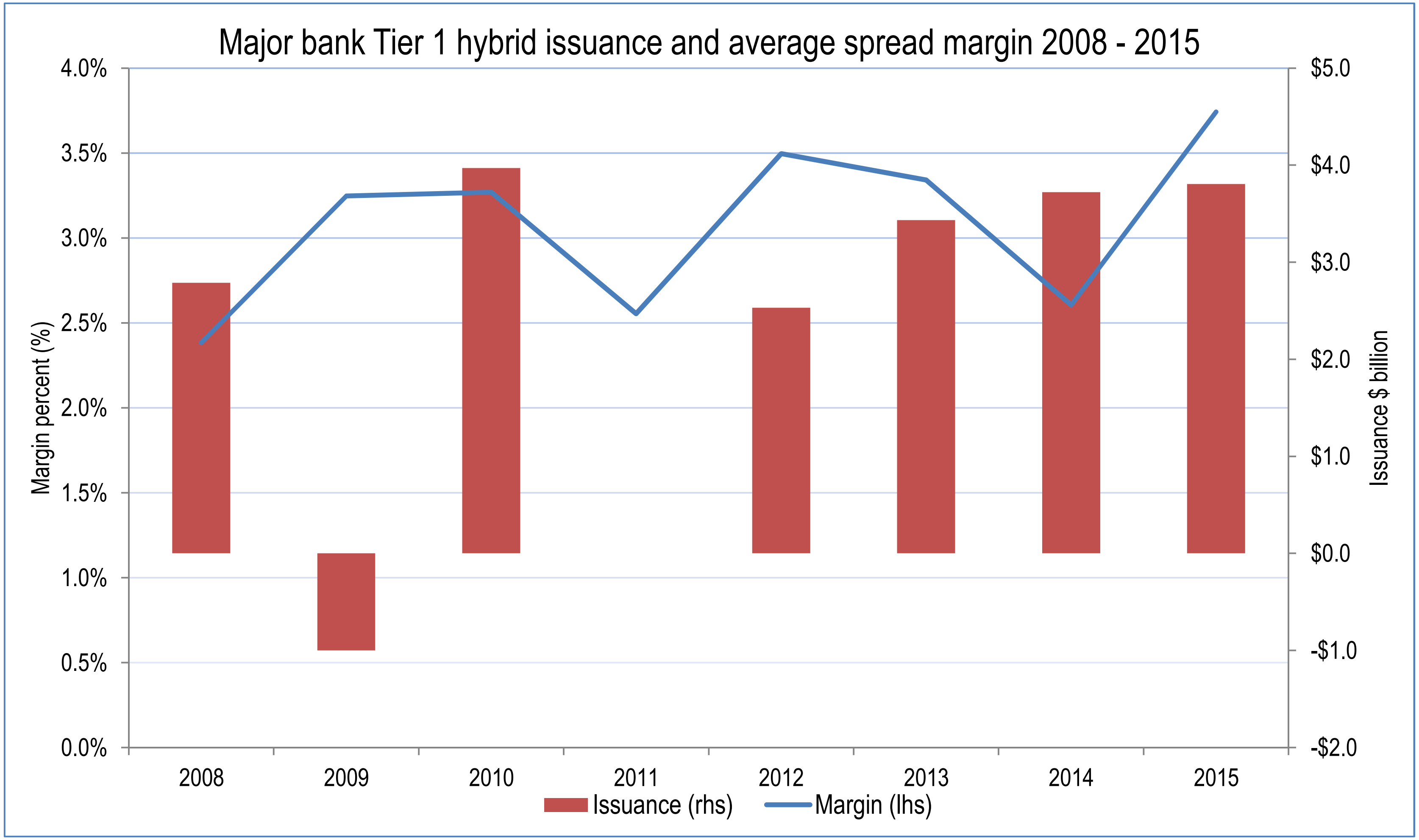
Fund performance

- While the Fund's performance was disappointing performance was broadly inline with that of the market over the 12 months to end 30 June.
  - The Fund's total return was 0.71% (market return was 1.01%).
  - Fund total return comprised;

	Cents per unit (cpu)
Change in capital value	<0.42>
Income (Dividend	0.40
Franking benefit	0.063

- Poor performance of the Fund and the market at large was a function of;
  - IPO supply and
  - Non IPO supply.

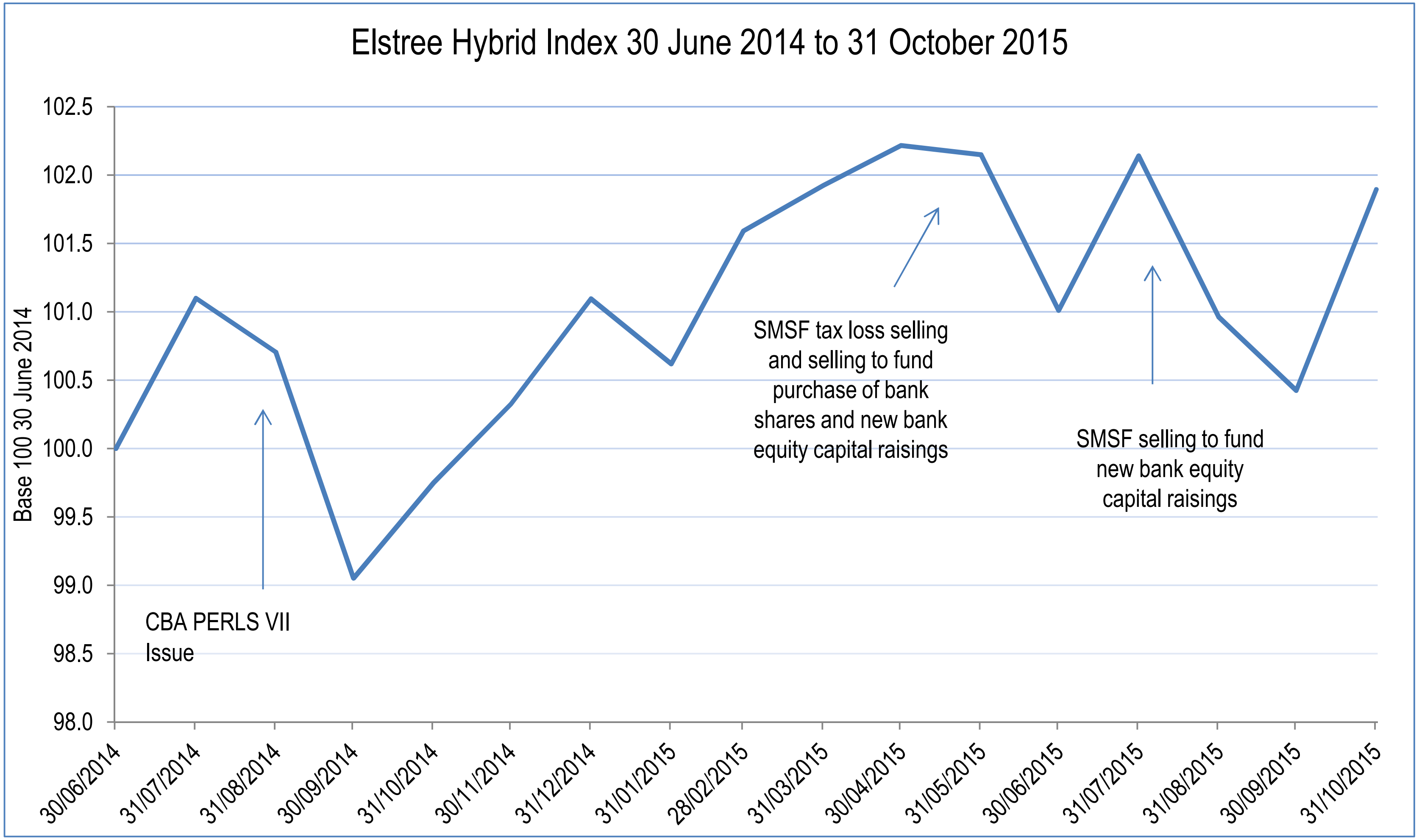
Record IPO Basel 3 compliant Tier 1 hybrid supply a factor



Elstree Investment Management Limited

Source: Elstree & ASX

....so too are non IPO factors – bank equity capital raisings



Source: Elstree Hybrid Index

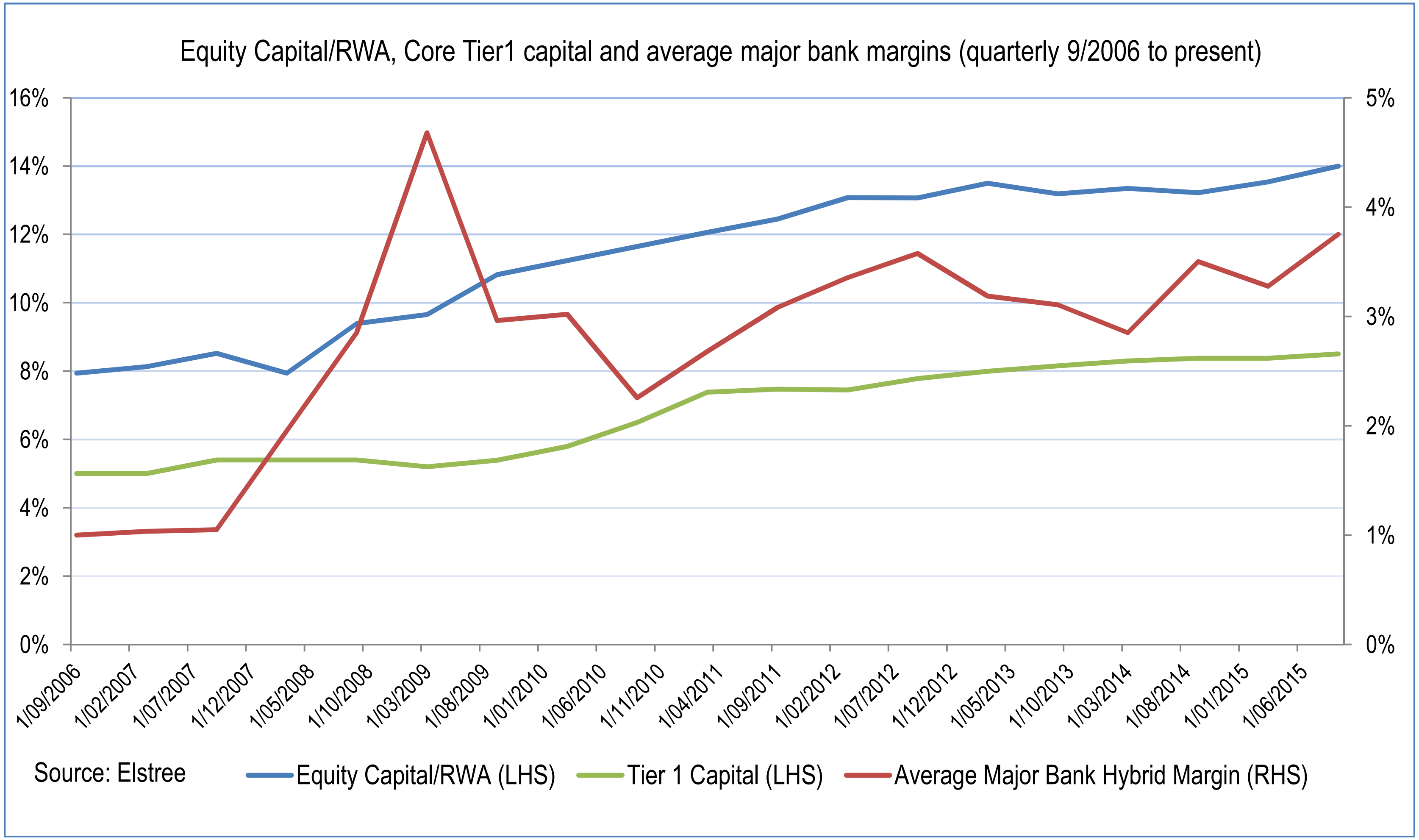
What can we expect?

- Spread margins, which move in the opposite direction to price, are currently as wide as they have been since the GFC.
  – The supply factors that contributed to spread margins widening to current levels are expected to dissipate over the next 12 – 18 months.
    - IPO supply expected to be half what it was in FY2015.
  – Demand expected to increase as;
    - SMSF retirees contemplate lower cash and TD rates amid continuing equity market volatility and
    - Investors recognise the latent value in hybrid capital instruments.
  – While the process will be protracted a combination of these factors is expected to narrow spread margins significantly over time.
    - We estimate the fair value spread margin of the market at large to be around half what it currently is.

What can we expect?

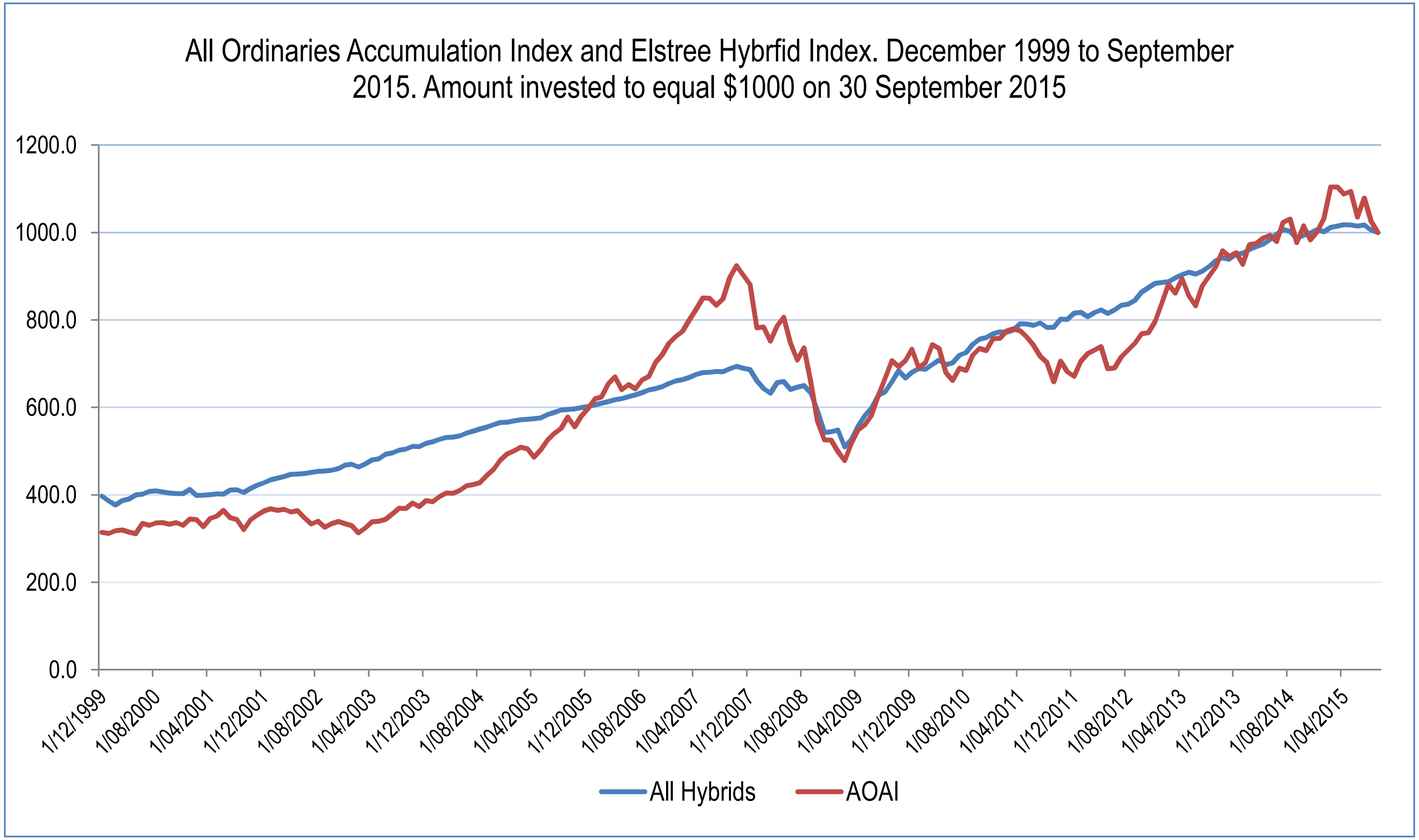
- Banks, who are the major issuers of hybrid capital instruments, are now better capitalised and more securely funded than at any time in their history.
  - This is not yet reflected in the spread margins of hybrid capital instruments which are as wide as they have been since the GFC.
    - Only a matter of time before investors recognise the de-risking of the banks and reprice hybrid capital instruments accordingly.
  - Portfolio well positioned in long credit term duration tier 1 hybrid capital instruments to capture maximum benefit from spread margin contraction.
    - Spread margin contraction of 100 basis points equates to a c4% increase in the capital value.
- Worst case return outcome of the Fund in CY 2016 is the income yield of c7.00% (assumes no change in the capital value or the NAV).
  - The total return outcome is limited (only) by the extent of spread margin contraction.

This doesn't make sense: More capital and wider margins



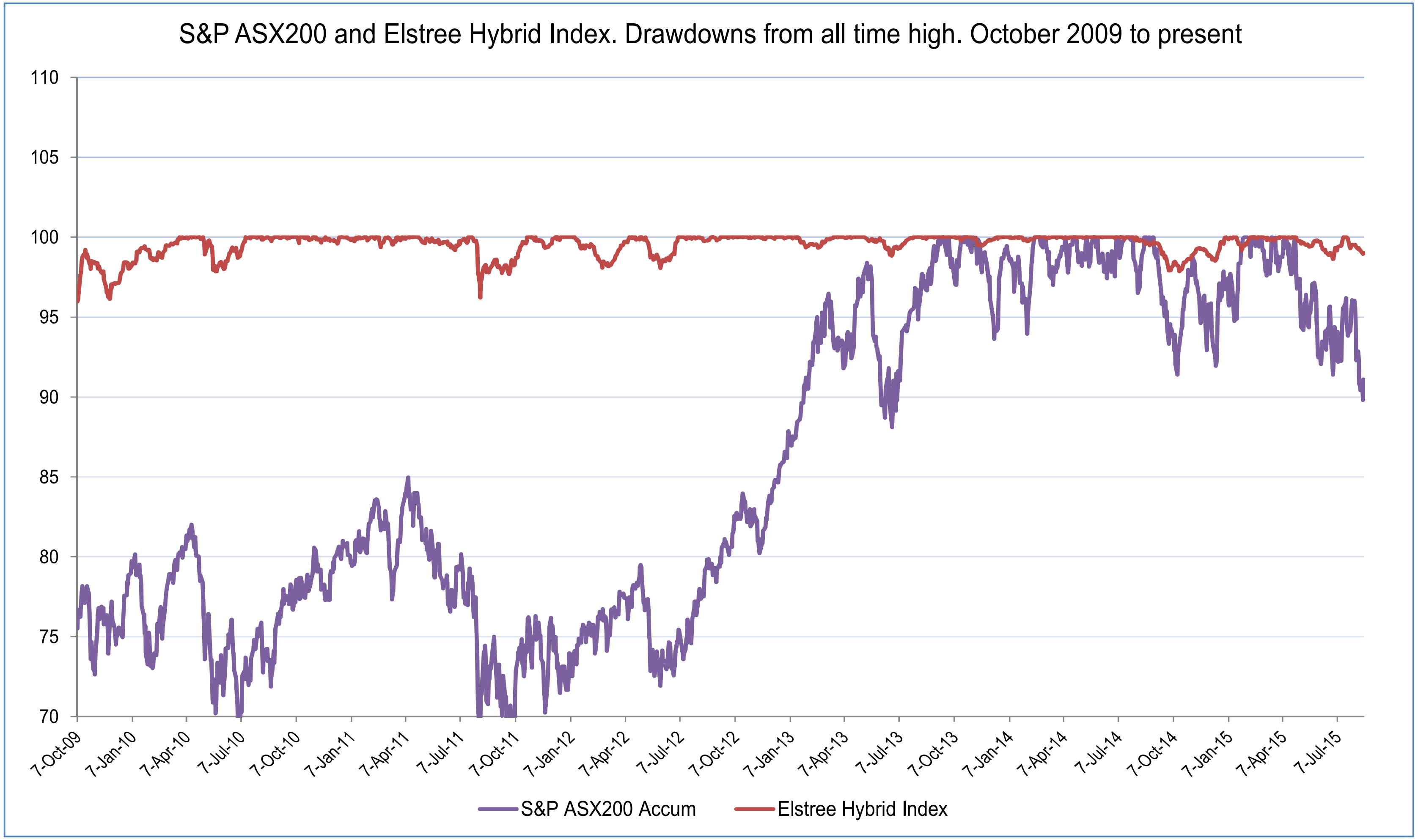
Source: Elstree

While comparisons are odious the case is compelling



Source: Elstree & ASX

Depth and duration of drawdowns - shallow and short



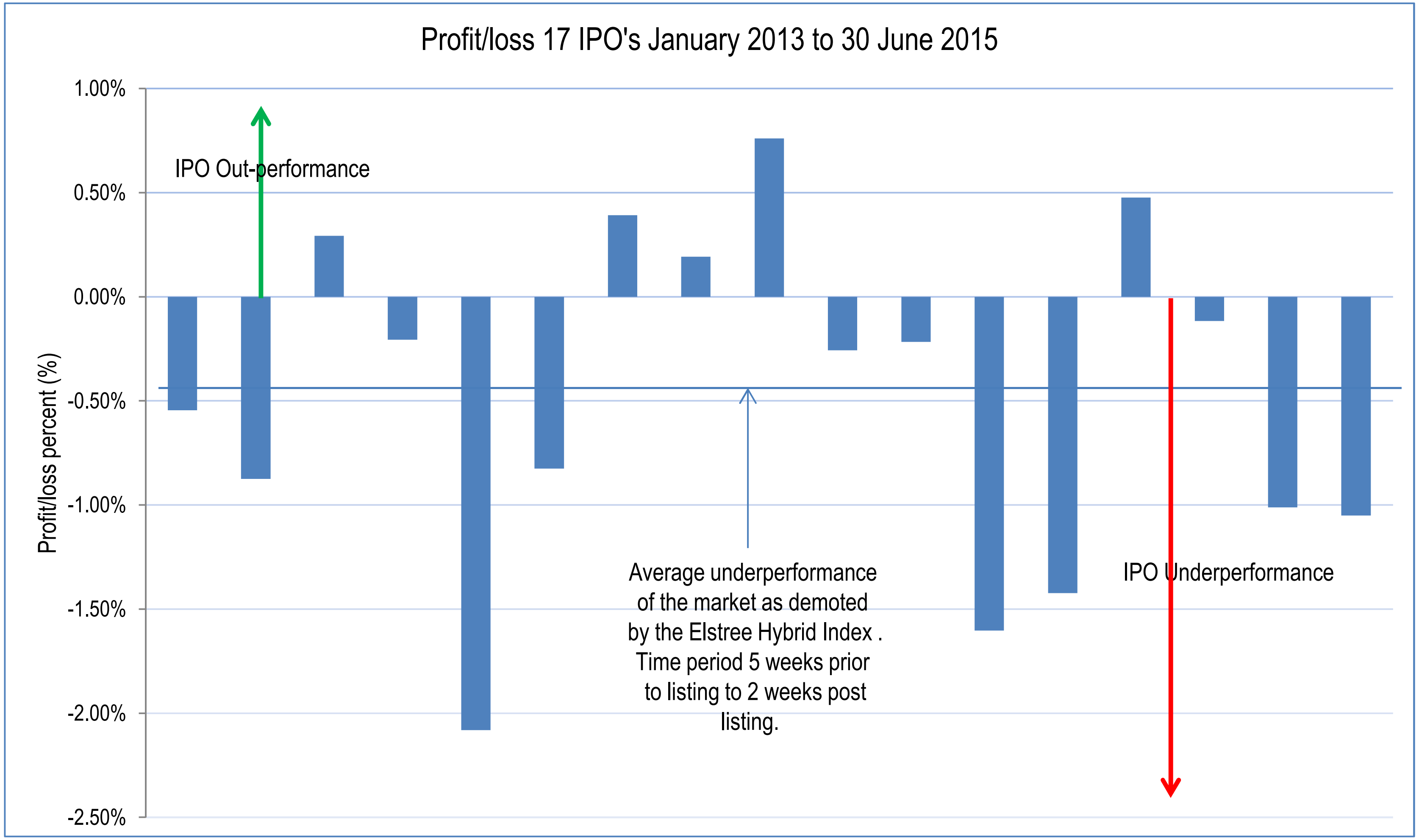
Source: Elstree

The case for using a managed fund rather than doing it yourself

Period % per annum	Fund	Top 10 securities by market cap	Bank Bill Swap Rate UBS (A)
1 year	**0.12%**	0.08%	2.48%
2 year	**3.28%**	2.24%	2.56%
3 year	**4.96%**	4.13%	2.74%
4 year	**5.76%**	4.46%	3.13%
5 year	**5.59%**	5.20%	3.51%

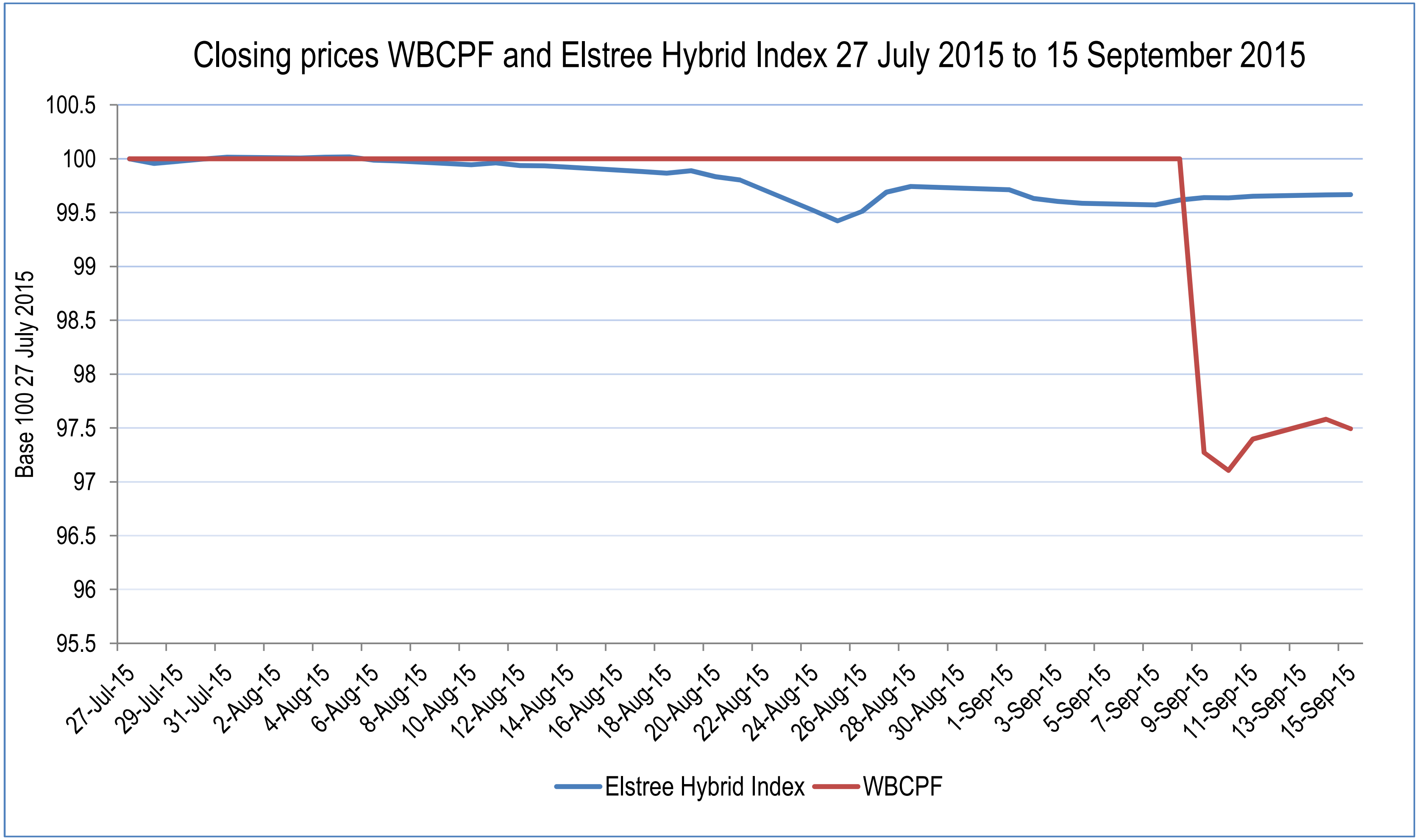
Returns are gross of franking and net of fees. Returns are to 30 September 2015

IPO risks are real and costly



Source: Elstree & ASX

IPO risks are real and costly – a recent example



Source: Elstree & ASX

About the manager

- Elstree Investment Management Limited (Elstree) is both the Responsible Entity (RE) and the manager of the Australian Enhanced Income Fund (Fund).
- Elstree has been managing portfolios of listed hybrid debt securities since 2003.
  - The investment managers have over 60 combined years experience managing portfolios of such securities.
- Securities are selected based on Elstree's 4 step filtered security selection process
- Securities are weighted in the portfolio based on their;
  - Level of cheapness,
  - Market capitalisation,
  - Credit rating and
  - Liquidity.
- Strong risk management emphasis with processes in place to measure and quantify market risk, liquidity risk and 'Black Swan' event risk.

Top 10 securities in alphabetical order

1	ANZPD
2	ANZPE
3	CBAPD
4	CNGHA
5	CWNHB
6	GMPPA
7	NABHA
8	NABPB
9	WBCPC
10	WBCPE