

FUND OUTLINE

The Fund is a concentrated long only equity Fund, investing in US listed stocks favoured by leading global fund managers. The Fund's objective is to outperform its benchmark by 3-5% pa over any rolling 5-year period. Preservation of Capital is a key tenet of the Fund, and a strict dynamic risk control strategy is in place to control losses, to enable optimal long-term compounding within the Fund.

MAY COMMENTARY

The Fund made 5.92% in May and has returned 32.68% since inception (19.55% annualised).

May was another strong month for the Fund, outperforming the benchmark by over 2.5%, bringing the year's outperformance to 13.78%. Our top performing stock this month was MercadoLibre (MELI), up 46% for the month. MELI is Latin America's e-commerce and digital payments leader, and has a market leading position in each of the 18 countries it operates in.

This month we are going to look a little deeper at what drives long term returns. It will be a bit longer than normal and have a bit more math than normal. This idea has been explored in depth by a new finance blogger (www.breakingthemarket.com), a really excellent blog, well worth spending some time on, and I will attempt to do a short piece covering the main points.

Lets dive in. Imagine you must choose between 2 games:-

1 - You have to bet \$100, and have a 50% chance of winning \$50, and a 50% chance of losing \$40. The expected outcome of the game is a positive \$5. Each round you can only bet \$100.

2 – You start off with a \$100 bet, same odds, but each subsequent round you must bet your full amount remaining after the preceding round.

At first glance you would possibly pick game 2, as you can play forever, compound your winnings, and retire rich. Game 1 seems good, but your winnings are limited.

Counterintuitively this is not the case. If you choose Game 2, and play for long enough you are destined for ruin, and Game 1 will make you money (but not a lot).

The difference between the two games is that game 1 will return the ARITHMETIC average (\$1.05), and game 2 over time will return you the GEOMETRIC average (\$0.949) ($\text{SQRT}(1.5*0.6)$). This is because the result is multiplicative, not additive, as each round you must bet your full purse in game 2.

The 2 different returns are related by the following formula:-

Arithmetic average – (Volatility*Volatility)/2 = Geometric Average

The geometric average is the return you are getting in the long run, so how do we go about maximising that return? Looking at the formula we can do that by 1 – INCREASE the Arithmetic average, and 2 – DECREASE the volatility. (sometimes referred to as the volatility drag).

Increase the arithmetic average

This is where most people would focus all their attention, which is a mistake. At GANE we attempt to increase this number by building a dynamic, concentrated portfolio of stocks chosen by the best in the industry.

Decrease the volatility

This piece of the puzzle receives a lot of attention at GANE. We decrease volatility by:-

- Monthly rebalancing of the portfolio. Each stock represents 5% of the portfolio, and if it moves up or down because of monthly moves the stock gets rebalanced back to 5% at month end – more similar to game 1 than game 2.
- Risk management – We use a moving average to manage our risk. Below a certain moving average that stock will move to cash. While we do not use the 200 day moving average (but similar), in a study going back to 1928 the volatility of the S&P above the average was 14.6%, and below the average was 24.6%. The general principle is that below the moving average the volatility is far higher, and by moving to cash in these times we reduce volatility. ([here](#))
- AUDUSD FX rate – The AUDUSD generally moves opposite to stocks. If stocks are selling off generally so is the AUD, and because we are invested in USD stocks and do not hedge currency risk this works very well in reducing volatility (as witnessed during the Covid-19 sell off)

This whole concept goes very deep, takes time to wrap your head around and is not well understood. The whole idea of the mathematical difference between playing a single game (arithmetic average), versus playing a single game repeatedly (geometric average) is crucial. Some more ideas that can help bring the concept to life:

- Nassim Taleb's example – if you and five people play a game of Russian Roulette simultaneously, you have an 83% chance of living. If you play 6 games back to back, you have a 100% chance of not making it. This is the difference between the Arithmetic and Geometric average.
- Winning 25% twice outperforms winning 50% once then 0% (reduce volatility).
- Losing 50% of your money means you must win 100% to get back to breakeven (ouch).
- Win 10% and then lose 10%, what are you left with? It is 99% - our brains are not used to thinking geometrically.

As I mentioned before all these ideas are taken from, and laid out in a lot more depth in www.breakingthemarket.com. My apologies if my explanations are not clear, I am not a mathematician, but as an investor it is well worth the time to explore and understand the subject.

And all the above also helps to explain why the following quote rings so true.

And as always....

“Good investing isn't necessarily about earning the highest returns, because the highest returns tend to be one-off hits that kill your confidence when they end, invariably with large losses. It's about earning pretty good returns that you can stick with for a long period of time. That's when compounding runs wild.” - unknown

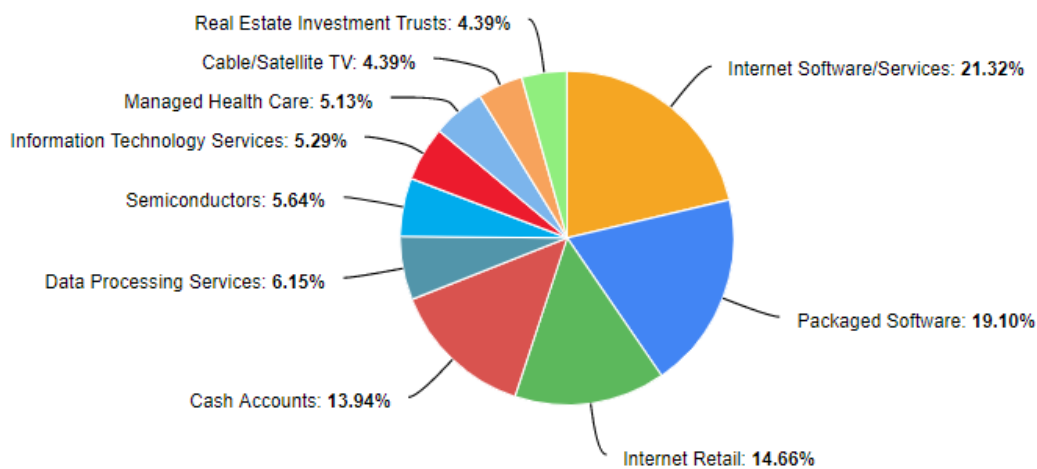
Please see next page for Charts and tables.

FUND FACTS

Inception	01 November 2018	Sharpe ratio	1.27*
Fund Size	2.551mm	Sortino Ratio	2.94*
Minimum Investment	AUD 50,000	Mid-Price	1.3268
Management Fee	Nil	Best Month	8.95%
Performance fee	15% of any returns above 6% pa	Worst Month	-3.9%
Other Fees	Any direct costs + 0.4% Buy/Sell spread	Website	www.ganecapital.com

*ratios are calculated before Fees & Expenses

PORTFOLIO BREAKDOWN



PERFORMANCE SUMMARY

GANE CAPITAL International Equity Fund	May-20				
	1 Month	Year to Date	3 year(p.a.)	5 Year(p.a.)	Inception(p.a.)
GANE CAPITAL	5.92%	14.18%	N/A	N/A	19.55%
BENCHMARK - Index	3.26%	0.40%	N/A	N/A	13.90%
BENCHMARK - Hedge Fund	1.71%	-1.69%	N/A	N/A	3.74%

