

MID YEAR REVIEW 2017-2018

Our purpose is to assist you to **protect and grow your investments** and **benefit from times of uncertainty**.

- Protection is always in place with upside
- Riding out the storm
- Making money when others don't

If you act now, you won't be at risk of large losses on share market falls.



Historical context – prepare now to protect gains and benefit from times of uncertainty

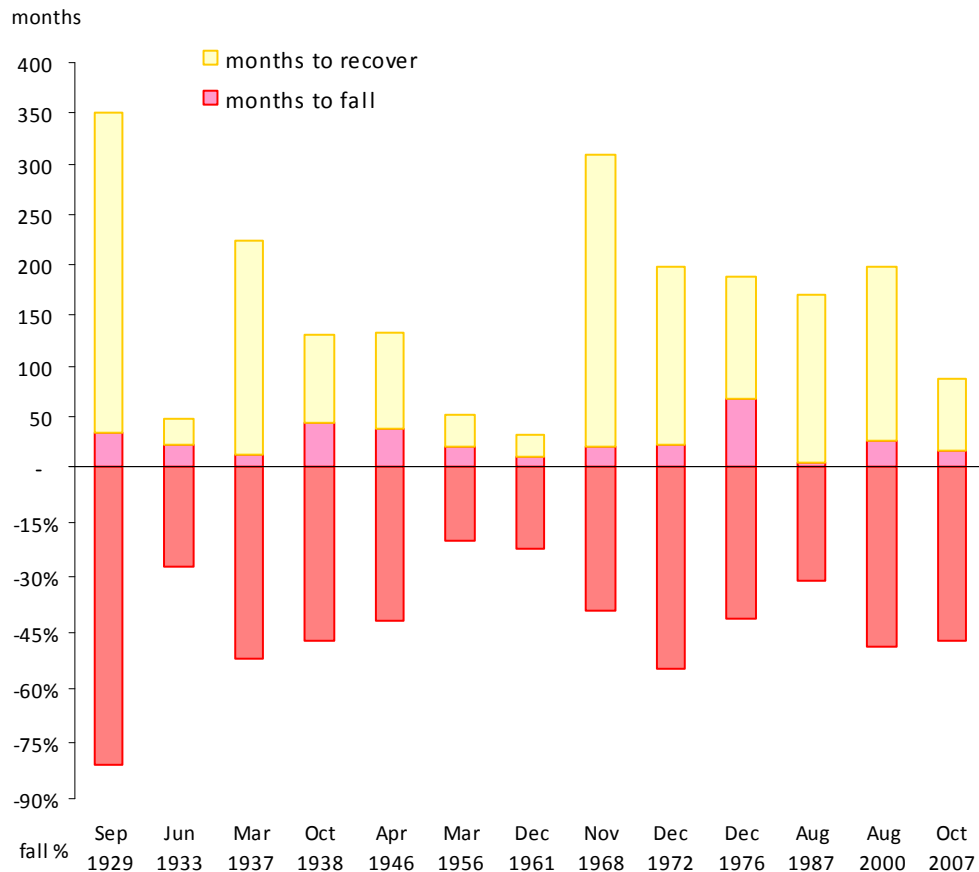
Major stock market corrections occur frequently. When stock market falls do happen, they typically happen very quickly and take years, even decades to recover to previous levels. Since 1927 stocks markets have fallen over 20% on 13 occasions. The range of falls and duration has been -20% to -81%, with declines happening over a period from 3 to 67 months.

The last stock market correction was over 9 years ago.

The graph below shows the extent of falls from peak to trough, the duration of the fall, and time taken to recover to pre fall highs.

S&P 500 Index - 90 Year Historical Chart

Peak to trough falls > 20%, duration of falls, time to recover to pre fall levels



Source: <http://www.macrotrends.net/2324/sp-500-historical-chart-data>

Macro trends interactive chart of the S&P 500 stock market index since 1927. Historical data is inflation-adjusted using the headline CPI and each data point represents the month-end closing value.

Sequencing risk –major falls matter more near or early in retirement

Returns have more impact at some points in your investment lifecycle than at others. Sequencing risk is the risk that markets fall near or early in retirement. The wrong sequence of returns can have a big impact on your retirement portfolio. Negative investment returns early in retirement can be particularly damaging. Our investment approach is of particular benefit to pre or post retirees who don't have the time required to overcome investment losses if there are large market falls.

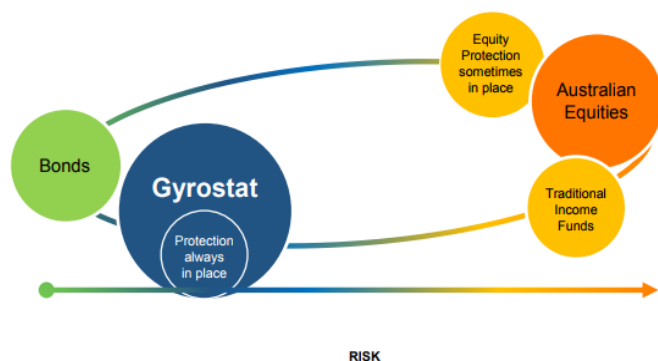
Gyrostat Absolute Return Income Equity Fund

Our Absolute Return Fund is a 'conservative' asset combining protection, returns and regular income. Our distinctive investment approach always has protection always in place with upside – for 7 years we've had no quarterly draw-downs exceeding 2%. We prefer changing markets (more trending and volatile conditions, particularly large 'one off' market falls.)

Gyrostat Absolute Return Income Equity Fund

Asset allocation solution – adjusting the portfolio mix

Protect and grow capital with reliable income through the complete investment cycle



Investment Objectives:

- **Returns:** 6% - 8% pa in trending markets, greater than 8% pa in volatile markets, short term bond returns in stable markets
- **Income:** Minimum **cash rate + 3%** paid semi-annually (currently 4.7% p.a.) from dividends and franking credits
- **Protection:** No quarterly NAV draw-downs exceeding 2%

Our strategy exploits the differing levels of 'implied volatility' in the option market from differing maturities, or within the same maturity across a different range of strike prices. This has been observed by academics and market participants for many decades.

Technology enables our proprietary software systems to construct a volatility term structure and identify the 'least cost' call and put option alternatives available in the market at that time. There are many series to choose from. This is reflected in differing levels of 'implied volatility' across time periods and within a range of strike prices within the same time period. Gyrostat uses a variety of bought option and other strategies typically ranging from duration of 3–15 months, depending upon the prevailing option market conditions.

With market movements, the "options" component needs to be re-set or actively managed to ensure that the risk-return parameters meet the investment charter. This involves the buying or selling of options.

A video with brief slides outlining of our investment approach and track record is available at:

Gyrostat Absolute Return Income Equity Fund - in depth guide

Current state of the market: "Incredible risks yet bullish trend persists"

Investment features:

- Protection always in place with upside (participate in the upside in rising market)
- Make money in changing markets (prefer more volatile conditions, especially if large 'one off' market falls)
- Proven strategy over 7 years – our innovation is the investment risk management of equities
- An Absolute return Income Equity fund is a conservative asset with the potential for capital growth in rising and falling markets

[Download PDF for more information](#)

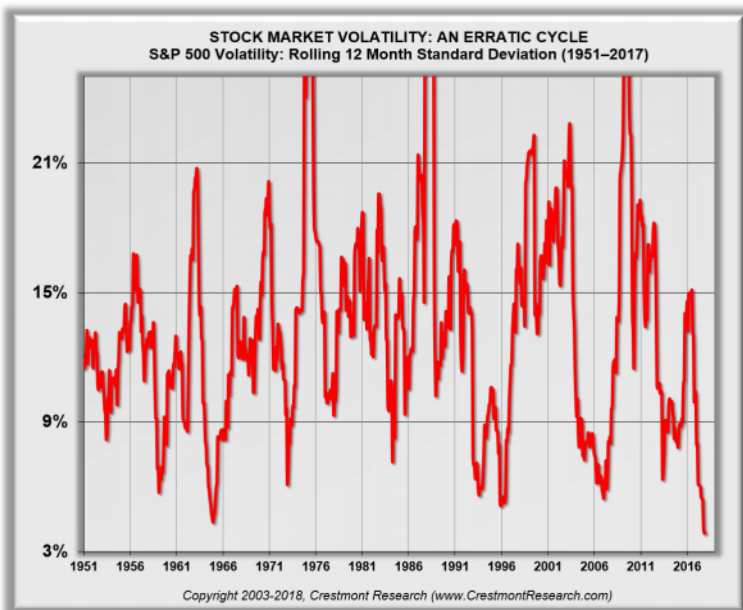


<http://www.gyrostat.com.au/news/gyrostat-absolute-return-income-fund-in-depth-guide/>

REVIEW OF HALF YEAR PERFORMANCE

Volatility during the half was at historically low levels. At this stage of the cycle our returns are as guided – at the lower end of the range. The more market volatility, the more opportunities we have to increase investor returns. This continues the trend of falling volatility, which has accelerated over the past 3 years.

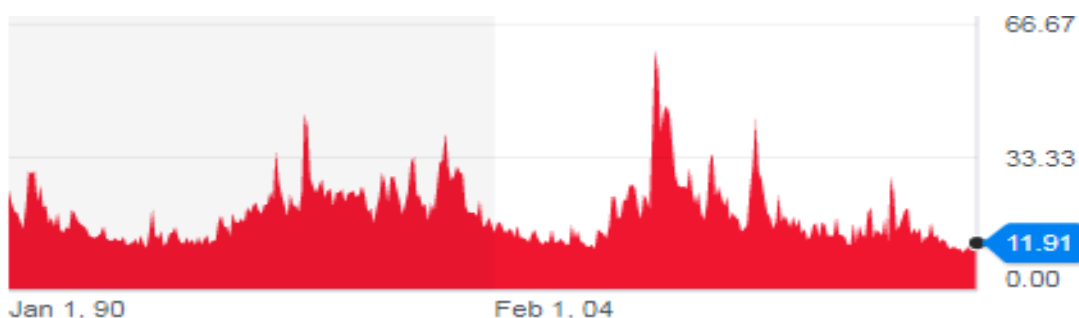
Figure 1. S&P 500 Index Volatility: Rolling Volatility (1950 to Present)



Source: <https://www.crestmontresearch.com/docs/Stock-Volatility-Perspective.pdf>

Historically ‘low’ volatility environments have been of around 4-5 years duration before entering a more volatile phase. The current ‘low’ volatility phase commenced in 2012.

VIX index 1990 – current



A mid year distribution of \$ 0.01975 per unit was declared (at an annualized distribution of 4.7%) comprising \$ 0.01382 cash and \$ 0.00593 franking credit.

A statement of holdings is attached detailing the distribution and your investment balance.

Outlook

We anticipate that volatility will return to more 'normal' levels as a result of geopolitical events and changes in Central Bank policies (less liquidity with higher interest rates as quantitative easing unwinds).

We agree with the views of Noble Prize winning economist Richard Thaler. He is nervous about stock markets and has misgivings about the low volatility of markets and the continued optimism amongst investors.



<https://www.bloomberg.com/news/videos/2017-10-10/nobel-winner-thaler-is-nervous-about-low-volatility-video>

Similar views are expressed by Stephen S. Roach, former Chairman of Morgan Stanley Asia and the firm's chief economist, a senior fellow at Yale University's Jackson Institute of Global Affairs and a senior lecturer at Yale's School of Management.

Complacency Will Be Tested in 2018

Dec 14, 2017 | **STEPHEN S. ROACH**

Despite seemingly robust indicators, the world economy may not be nearly as resilient to shocks and systemic challenges as the consensus view seems to believe. In particular, the absence of a classic vigorous rebound from the Great Recession means that the global economy never recouped the growth lost in the worst downturn of modern times.

<https://www.project-syndicate.org/commentary/test-for-economic-complacency-in-2018-by-stephen-s--roach-2017-12>

A COMPELLING OPPORTUNITY – GYROSTAT ASX200 DOWNSIDE PROTECTION FUND

The good news from historically low volatility is the costs to protect your ASX 200 investments are the lowest since 1950.

We are launching the Gyrostat ASX200 downside protection fund to enable you to protect your portfolio of Australian shares against large one off falls and large losses.

The fund uses our established investment approach and is designed to increase in value with ASX200 market falls, particularly large market falls, whilst not capping upside should the markets continue to rise.

As an illustration, an investment of 5% of the underlying exposure, or \$ 50,000 into the Gyrostat ASX200 downside protection fund, protects a \$ 1 M underlying ASX 200 holding against large one off falls and large losses.

If you act now, you won't be at risk of large losses on your Australian share holdings from large share market falls.



<https://www.youtube.com/watch?v=Qbe79zWjWg>

To thank our existing investors for your support with our existing fund, we will be offering 'attractive terms' to you as the fund is launched.

We anticipate writing to you in February 2018 with further details when the ASX 200 downside protection fund is launched.

Yours sincerely



Craig Racine