SIGMA FUNDS MANAGEMENT®

Sigma Australian Shares Strategy

Monthly update as at 30 June 2015

	Month %	Quarter %	1 year %	2 years % p.a.	3 years % p.a.	4 years % p.a.	Since Inception^ % p.a.
Sigma Australian Shares Strategy*	(6.5)	(4.6)	7.0	13.0	17.1	9.8	4.6
S&P/ASX 200 Accumulation Index	(5.3)	(6.5)	5.7	11.4	15.1	9.2	2.7
Value added (detracted)	**(1.2)**	**1.9**	**1.3**	**1.7**	**2.1**	**0.6**	**1.8**

**Gross Performance. Past performance is not a reliable indicator of future performance. ^Since Inception: 1 July 2007†*

Key points

- Significantly overweight Diversified Miners and underweight Major Banks
- Cyclical sectors expected to benefit as earnings bottom and risk appetite increases
- Fund positioned for cyclical re-rating and away from lower return defensives

Individual stock performance of note

The Fund *underperformed* a declining market in June. Outperformers of note related mostly to stocks that held their ground as the market fell. Bendigo and Adelaide Bank and Macquarie Group were essentially flat in the month and by default outperformed. Weakness in major index heavy weights, Wesfarmers (-10%) and CSL (-8%) on no news were the top contributors to performance in a relative sense. Stock detractors related mostly to media stocks after Nine Entertainment (-27%) fell post downgrading EBITDA guidance by 8%, citing a softer free to air advertising market, however specific programing issues are the more likely cause in our view. Notwithstanding, Seven Media (-18%) and APN News & Media (-16%) all fell, with APN weakening for the third month in a row post the takeover speculation. The absence of Commonwealth Bank (flat) and Telstra (-1%) detracted from performance in a relative sense.

The S&P/ASX 300 Accumulation Index was down (-5.3%) in June, its worst monthly performance since May 2012. For the financial year 2015, the Australian Equity market ended up (+5.6%) mostly as result of dividends paid. Gains over the course of the month were swallowed up by a month-end sell-off as global investors reacted to news of a breakdown in negotiations between Greek Prime Minister Alex Tsipras and the nation's creditors, increasing the likelihood of an exit from the currency union. In response to a "run on banks deposits" the Government imposed capital controls and shut banks, limiting daily cash withdrawals to 60 euros per day. The missed interest payment (Euro $1.6bn) to the IMF on Tuesday, 30 June may eventually result in Greece becoming the first developed country to default to the IMF.

Economic data out of the US painted an increasingly positive picture, adding support for a September "interest rate lift-off". The Q1 economic contraction was less severe than first thought (-0.2% vs -0.7% estimate), labour market data revealed another strong month of jobs growth as well as signs of wage pressure emerging, and consumer spending posted its strongest gain in nearly six years (+0.9% in May). Equity markets responded negatively to heightened prospects of interest rate rises, the S&P500 closing (-2.1%) lower, and bonds sold off with 10 year yields backing up 23bps to 2.35%.

The Chinese equity markets volatile ride continued with the Shanghai A shares index rallying 12% by the June 12th, to end up down -7% for the month after rallying 5.5% on the final day to be up +109% for the financial year. The Chinese authorities announced the countries pension funds would be allowed for the first time to invest in stocks.

On the domestic economic front, stronger than expected jobs growth (steady participation and a surprise fall in the unemployment rate to 6.0%) continued for the second consecutive month. The RBA left the cash rate unchanged in June at 2.0%, although the central bank noted that further depreciation of the AUD was "both likely and necessary" to continual rebalancing the economy. Locally, the Market ex Resources (-4.8%) outperformed Resources (-9.1%) aided by a resilient Bank sector (-2.3%). The Consumer Discretionary sector was the weakest performer this month, although all sectors were in the red. Small Caps underperformed the ASX 100 (-5.1%) by 2.7%. Both Small Industrials and Small Resources underperformed their Large-Cap counterparts by -2.7% and -2.3% respectively.

Portfolio changes and outlook

Australian Shares *relative* valuation upside currently stands at 32%, a since inception high. The portfolio currently has 32% upside relative to the market which is fairly valued in our view (see graph). While the portfolio remains attractive on

valuation grounds, our *business risk metrics* are the *least attractive* since inception. This has been the case for some 18 months, and as communicated in our quarterly strategy reviews we fully expect more volatile outcomes relative to market (as recent performance indicates), however we continue to believe the *valuation upside* will more than compensate for the volatility.

While Nine Entertainment (NEC) cited a softer free to air market as the reason for the downgrade, we suspect the reliance on a fewer number of shows as the more likely cause. Seven West Media (SWM) added weight to this view when guidance was reaffirmed during the month. However the market has taken a more negative stance, pursuing a "structural thesis" due to the entry of online streamlining services Netflix and Stan. Accordingly all three media stocks fell by 26% on average during the June Quarter (NEC -26%; SWM -24%; APN -29%). However, we believe the market is substantially overplaying the extent which these new services will eat into the advertising revenue of the major free to air television networks. Anti-siphoning laws regulating media companies access to significant sporting events remains the substantial barrier to entry, and we believe the overseas experience of free to air television networks is unlikely to be repeated in Australia

As a group, these stocks have an average weighted PE of 7.6 and fully franked dividend yield of 7.8%. Furthermore, all have significantly de-geared their balance sheets over recent years. In NEC's case, the company "net cash" position is being returned to shareholders through ongoing buybacks.

Much improved balance sheet positions, strong cash-flow generation, substantial discounts to valuation (NEC 75%; APN 80%, SWM 122%) and a clear market perception differential lead us to add to all three during the period.

Stocks Added

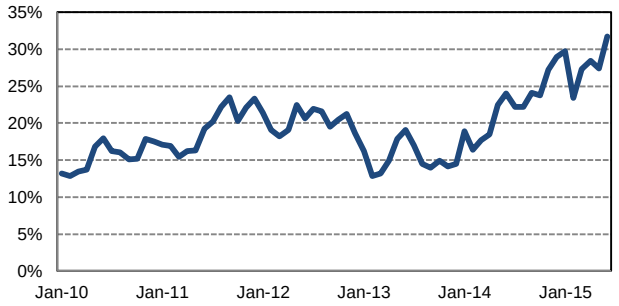
Nil

Stocks Sold

Nil

Australian Shares : Relative Valuation Upside

Source: Sigma Estimates, IRESS



Pricing Metrics	1-Yr PE	Net Div. Yield	Price/ Book Value	Price to NTA
Australian Shares	16.4	4.2%	1.3	2.0
S&P/ASX 200	17.3	4.3%	1.9	2.7
Date	**Jun-15**	**Jun-14**	**Jun-13**	**Jun-12**
Stock Numbers	26	27	30	37
Active Share	68.5%	60.2%	47.6%	49.9%

Source: Sigma estimates, GS Portfoliowise

Top 10 active positions

Stock	Active weight%
Largest overweights:	
Harvey Norman Holdings	4.8
Rio Tinto	4.4
AMP	4.4
Bendigo and Adelaide Bank	4.3
Qantas	4.3
Largest underweights:	
Commonwealth Bank	10.0
ANZ Bank	6.4
Telstra	5.4
Westpac Bank	3.2
Wesfarmers	3.2

Note: Active weights refer to positions above benchmark only.

Asset allocation

Sector	Active weight %
Materials	6.2
Consumer Discretionary	5.9
Financials ex-Real Estate	5.0
Energy	2.4
Information Technology	(0.8)
Utilities	(1.7)
Industrials	(2.3)
Consumer Staples	(3.4)
Health Care	(4.8)
Telecommunications	(5.1)
Real Estate	(6.6)
Cash & Other	5.2

Note: Active weights refer to positions above or below benchmark.

Strategy summary

Australian Shares combines the highest conviction stock ideas from Sigma's Large Cap investment team driving superior performance, lower risk and increased consistency of returns.

Australian Shares - Competitive Advantage

- Deep and rigorous fundamental analysis of companies and sectors
- Thorough ongoing peer review by a very experienced team of investors
- Investing with conviction in a focused portfolio of undervalued businesses
- Putting aside benchmarks to allocate capital with the aim of achieving the stated return objective

Contact

For more information contact Pinnacle Investment Management, the Fund's distributor, on 1300 010 311.

See also www.sigmafunds.com.au

Sigma's Differentiated Business Model: 'Integrated & Aligned Investment teams'

- Most investment management firms comprise distinct Large Cap and Small Cap teams with separate incentive structures and competing interests
- In contrast, Sigma's Large Cap and Small Cap teams are equal partners, completely aligned to success of the Sigma's investment strategy's
- Sigma Australian Shares strategy is enhanced by an integrated investment approach of an experienced investment team

About Sigma Funds Management

- Value-style Australian equities manager which aims to outperform without the downside of "value traps" through an investment approach called *Value: Risk Adjust*
- Independent and majority employee-owned firm founded in 2009 by six experienced investment professionals who previously worked together at a leading global investment manager

† Since Inception performance includes 22 months at a former investment manager plus median value manager performance for transition period prior to setting up Sigma.