November 10, 2016

Australian Enhanced Income Fund - ASX Code "AYF"
October 2016 Investment Update and NAV

October 2016 NAV and Fund performance

The Fund's NAV of a unit at the close of business on October 31, 2016 was $**5.94** per unit. This compares with the ex-distribution NAV of a unit at the close of business on 30 September of $5.883. The change in NAV over the month of October represents a return of 0.98%**.** The franking benefit for October was estimated to be **0.04%**.

Performance	1 month	3 months	12 months	3 Year p.a.
Australian Enhanced Income Fund*	0.98%	2.11%	5.09%	3.56%
UBS(A) Bank Bill Index	0.15%	0.46%	2.14%	2.41%

*Returns do not include the benefit of franking. Past performance is not necessarily a guide to future performance.

Relative performance

- The ASX listed hybrid sector returned 1.05% for the month. This compares with the All Ordinaries Accumulation Index return of (2.18%) and the UBSA Bank Bill Index return of 0.15%.

Fund performance

The Fund performed broadly in-line with the market this month. The Fund's rolling 3 year annual net return, which excludes the benefit of franking but is net of all fees, for the period ending 31 October 2016 increased to 3.56% from 3.49% previously.

Asset class return comparisons

We thought it might be timely to compare asset class returns over the last 10 years as investors begin to think that about the possibility that interest and bond rates have most likely bottomed. While the 'lower for longer' scenario is entrenched in investors psyche and looks for all intense and purpose as though it will play out, it is the bond locomotive that has helped drive asset prices higher since the mid 1980's that has arguably run out of steam. This is by no means the end of the world but it does mean investors have to be a more circumspect with where they allocate their investment $.

The table overleaf explained. The outcome contradicts traditional thinking

The rainbow coloured table overleaf shows the returns for a number of asset classes by year and rank since just before the GFC to the present. The colours of each asset accord with the asset's ranking over each year, for example, Listed Property in red was the number 1 performer in 2012, 2014 and 2015, while Hybrids, in purple was the best performer in 2010 and is the best performer 2016 year to date. The column without any colour is the annualised return over the period. Typically, you find that the more volatile and highly identifiable asset classes do particularly well one year and not so well the next, with the more defensive asset classes simply 'chiselling' away. On average, you'd expect riskier asset classes to generate higher than average returns to make up for their riskiness with the safer, less volatile ones returning below average. The data revealed in the table overleaf contradicts this thinking.

Australian Enhanced Income Fund (ARSN: 115 632 990)
Responsible Entity: Elstree Investment Management Limited (ABN: 20 079 036 810)
Level 10, 30 Collins Street Melbourne VIC 3000
Telephone: 61 3 8689 1348
Email: info@eiml.com.au

November 10, 2016

	Annualised	31/12/2007	31/12/2008	31/12/2009	31/12/2010	31/12/2011	31/12/2012	31/12/2013	31/12/2014	31/12/2015	Year to date
All Ords	3.8%	18%	15%	62%	13%	11%	33%	36%	27%	14%	7%
Listed Property	-0.2%	10%	8%	49%	10%	6%	30%	26%	10%	7%	6%
S&P/ASX200 BANKS	6.8%	7%	-21%	40%	6%	5%	19%	24%	9%	4%	6%
MSCI	1.4%	7%	-40%	27%	5%	-1%	14%	20%	6%	4%	5%
Bonds	6.4%	7%	-40%	25%	3%	-1%	13%	18%	6%	3%	4%
Cash	4.1%	5%	-42%	21%	0%	-8%	12%	8%	5%	2%	2%
Hybrids	5.2%	3%	-44%	8%	-2%	-11%	8%	7%	3%	2%	2%
Euro Equities	-2.9%	-8%	-54%	3%	-6%	-17%	8%	3%	3%	1%	-5%
Euro Bank	-14.6%	-9%	-64%	2%	-27%	-38%	4%	2%	1%	-3%	-6%
Euro CoCo	6.1%	n/a	n/a	n/a	n/a	n/a	n/a	n/a	-5%	-5%	-28%

What is the data telling us?

There are a number of interesting things about the data.
- Both Australian listed hybrids and Euro CoCo's have done better than average with AUD hybrids atop the charts in 2010 and 2016 year to date and having only one bottom quartile result (2015).
- Hybrids (both AUD and Euro) are sometimes correlated to bank equity returns, but more often than not, they are un-correlated.
- While we haven't shown much of the pre GFC period, listed markets have been less volatile since the GFC. Despite the alleged 'asset bubble blowing' caused by the zero interest rate policies of the global central banks the average difference between the top and bottom performing asset class is half that of the pre GFC period.
- While it is stating the obvious the way to good long term performance is to avoid the really bad years. Listed Property is a good example. It has 3 years atop the table and 1 runner up result, but the bad GFC years meant that its 10 year performance is flat (-0.2%), compared to Bank equity returns of 6.8% p.a. and hybrid returns of 5.2%.

Fund ready reckoner. Fund metrics and portfolio characteristics at a glance

	Sept 2016	October 2016
Net Asset Value (NAV)	**$5.883#**	**$5.94**
Change in NAV month on previous month (mopm)*	**(0.13%)**	**0.98%**
Total investment return includes the value of franking (mopm)	**0.08%**	**1.02%**
Dividend (declared October 2016 and payable 17 October 2016)	**$0.0875**	**n/a**
Percent franked (*quarterly estimate @ 30% tax rate*)	**37.37%**	**n/a**
Cash yield per annum (basis NAV)	**5.95%**	**5.89%**
Grossed up yield basis NAV per annum (*estimated*)	**6.80%**	**6.70%**
Investment grade issuer (including cash)	**90%**	**90%**
Fund average term	**3.7 years**	**3.6 years**
Bank Tier 1 exposure	**46%**	**44%**
Property exposure	**4%**	**4%**

* Returns do not include the benefit of franking. Past performance is not necessarily a guide to future performance. # Ex-Distribution

For additional information please contact **Norman Derham** at Elstree Investment Management Limited on (03) 8689 1348 or by email info@eiml.com.au While the information in this report has been prepared with reasonable care Elstree Investment Management Limited accepts no responsibility for any errors, omissions or misstatements however caused. This is general securities information only and is not intended to be a securities recommendation. This information does not account for your individual objectives, needs or financial situation.