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Magellan Global Trust

September 2017

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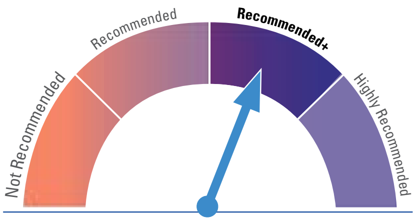
MAGELLAN GLOBAL TRUST

(expected ASX code: MGG)

Note: This report is based on information provided by the company as at September 2017

Rating



Key Investment Information	
Name of Fund	Magellan Global Trust
Investment Manager	Magellan Asset Management Ltd
Offer Open Date	29 August 2017
Broker Firm & General Public Offer	22 September 2017
Priority Offer	29 September 2017
ASX Trading Date	18 October 2017
IPO Unit Price	$1.50
Initial NAV	$1.50
Expected ASX Code	MGG
Distribution Policy	Cash distribution yield of 4% p.a.
Tracking Error	Benchmark unaware
FX Exposure	May range from fully hedged, partly , or fully unhedged
MER	1.35%
Performance Fee	10% of excess returns above hurdles

Fees Commentary

Fees are at the high end for a larger market cap global equities fund and more so when the performance fee is taken into account. However, we do note the 'payback' investors receive through several capital raising offer and ongoing structural fees of the Trust

Portfolio Characteristics	
Number of stocks	15-30
Stock limits	15%
Cash limit	0%-50%
Currency exposure	Active hedging 0%-100%

Note: This report is based on information provided by the Issuer as at September 2017

The investment opinion in this report is current as at the date of publication. Investors and advisers should be aware that over time the circumstances of the issuer and/or product may change which may affect our investment opinion.

OFFER OVERVIEW

The Magellan Global Trust (expected ASX code: MGG or 'the Trust') is seeking to list on the Australian Securities Exchange by raising a minimum of $250 million with no stated upper limit at an offer price of $1.50 per unit. The Trust will be managed by Magellan Asset Management Ltd (the Manager), a wholly owned subsidiary of the ASX-listed Magellan Financial Group Limited (MFG). It will be based on a high conviction, relatively concentrated global equities and benchmark agnostic mandate with a portfolio of 15 to 35 stocks. The investment strategy will be very closely aligned to the long running Magellan Global Fund (MGF) and will be managed by the same investment team, portfolio manager and according to the same investment methodology. The Trust has a distribution policy of targeting a cash distribution yield of 4% p.a. which is to be paid semi-annually. The Trust's distributable income will come from (1) dividends, (2) income from currency management and (3) realised capital gains. Should this be less than the 4% amount, the shortfall will be generated through the return of capital to unitholders (either through the return of capital growth or original invested capital) through a proportional sell down across the portfolio. In relation to total returns, we anticipate the Trust will be managed according to an internal target of long-term total returns similar to MGF, with a strong emphasis of downside risk mitigation. Currency exposure will be actively managed. MFG will bear all the costs in cash associated with establishing and listing the Trust.

INVESTOR SUITABILITY

The Manager's key focus is to deliver long-term average total returns similar to MGF with a strong focus on downside risk mitigation and the preservation of capital. The Manager will consistently pay a cash distribution of 4% p.a. which will no doubt appeal to certain classes of investors, including retirees. The latter class of investors will also be well served by the capital preservation focus. From a portfolio perspective, while not a mandated strategy, we would expect the Trust to at least initially exhibit its predominant exposure to the North American and European markets as well a material exposure to the technology sector on account of the Manager's emphasis on companies with sustainable long-term competitive advantages. Investors should note that the active currency hedging adds additional risk, with the potential for both positive and negative incremental returns. Historically, the Manager has generally outperformed in flat or falling market environments, with materially lower drawdown risk. The high conviction and concentrated nature of the mandate may mean that its returns and volatility may vary considerably to both its benchmark and its peers.

RECOMMENDATION

IIR ascribes a "Recommended Plus" rating for MGG. IIR holds the Manager in high regard, with a strong and stable team and investment committee, proven processes and strong performance track-record. Additionally, we are impressed with the Manager's approach, processes, and track-record in downside risk mitigation and capital preservation. Structurally, the Trust benefits from its listed status, a high degree of portfolio transparency, a 5% discount DRP plan, the priority offer to existing shareholders / unitholders, and the Manager's capital management initiatives to mitigate discount / premium to NAV risk. The offer structure creates a strong alignment with investors' interests, with MFG bearing all establishment and listing fees as well as effectively underwriting the priority offer to ensure non qualifying investors are not diluted and adversely impacted. On the flipside, we do identify several risks. Firstly, the return of capital component of the cash distribution does create a degree of market timing during market downturns (although the Manager has sort to minimise this by striking the 4% amount on the average rolling past 24 month period returns). Secondly, the fees are high for a large cap mandate, although we do note the 'payback' investors receive through MFG bearing all establishment and listing costs and underwriting the priority offer. Thirdly, there is a risk of downside pressure on the share price when the loyalty units escrow period expires.

SWOT ANALYSIS

Strength

- The Manager has a strong performance track-record, with the Magellan Global Fund consistently achieving objectives and generating alpha in the vicinity of 6% p.a. Impressively, most of the out-performance has been generated in material down markets, most notably in 2008 and 2011. The Manager has successfully preserved capital in significant down market environments.
- The offer structure has some strong positives for investors. Firstly, MFG is bearing all the establishment costs, resulting in the unit's NAV from first day of listing being equal to paid-in capital. Secondly, the Trust's priority offer provides a strong investment proposition for those who qualify for the loyalty bonus, but with the loyalty units to be funded by MFG, non qualifying investors will not be diluted.
- The Manager has sought to establish the distribution policy in order to provide greater certainty to unit holders on the value of upcoming distributions as well as address domestic investors' tendency to underutilise global equities partly due to lower distribution levels relative to domestic equities.
- The DRP is expected to be struck at a 5% discount to NAV. This discount will be funded by MFG, creating an attractive structure whereby those taking up the DRP are receiving a 5% bonus on their distributions while those who are not taking up the DRP and want the cash flow are not being diluted. The structure is inherently equitable.
- We note that the founder of MFG and co-portfolio manager of the Trust, Hamish Douglass, will be a significant co-investor in the Trust, creating a strong alignment of interest and indication of MFG's strong interest in the long-term success of the Trust.

Weakness

- The fees are high for a large cap mandate, although we do note the 'payback' investors receive through MFG bearing all establishment and listing costs and underwriting the priority offer (although this only benefits those that qualify under the priority offer);
- The return of capital component of the cash distribution does create a degree of market timing risk during market downturns in relation to the NAV of the Trust given the payment away of a part of the capital base of the Trust (although the Manager has sort to minimise this by striking the 4% amount on the average rolling past 24 month period returns).

Opportunities

- Access to a highly regarded investment manager with a proven investment process, strong performance track-record and a well-qualified and stable investment team;
- Domestic investors often exhibit a significant home country bias. The Trust provides the potential to address this as well as gain exposure to a range of sectors, industries, products, and services that may be very under-represented in the domestic market.

Threats

- Under the Priority Offer, eligible investors are subject to an escrow period, effectively ending on 11 December 2017. There may be both a percieved 'overhang' risk prior to this vesting date or a material increase in sell volumes subsequently as some investors seek to crystallise the 6.25% loyalty bonus, both creating the risk of downward pressure on the share price. It is difficult to confidently assess this risk at this point in time but, irrespective, it is likely to be a shorter term dynamic.
- Key man risk with Hamish Douglass is material. While Stefan Marcionetti is Co-Portfolio Manager, the investment strategy is very well defined and there are significant resources in the Investment Committee, Douglass plays a pivotal role in portfolio construction as well as the business as a whole.
- Foreign exchange exposure is actively managed. This introduces an additional degree of performance risk, both positive and negative, which is both an opportunity and a threat.
- LITs / LICs may trade at a discount/premium to NAV. This is both a threat and an opportunity, but provides an additional degree of risk over an unlisted vehicle.

PRODUCT OVERVIEW

The Manager is seeking to raise a minimum of $250 million at the offer price of $1.50 per unit. The Manager has not set an upper limit on the amount that can be raised under this offer and is keen to have FUM scale in order to assist investors with on-market liquidity.

The Manager adopts a long-term investment perspective and seeks to invest in high quality businesses with sustainable competitive advantages ('economic moat'). There is a strong emphasis on capital preservation, and it is in down market environments where the Manager has particularly shone historically and generated most outperformance. The investment strategy is high conviction, benchmark unaware with a relatively concentrated portfolio of 15 to 35 stocks (expected to be in the vicinity of 20 stocks). The Manager may have up to 50% portfolio exposure to cash, although it would only be in the most extreme of market environments in which the Manager would contemplate approaching such a level. Macro factors play an important part in managing the portfolio, specifically in assessing and aggregating factor risk within the portfolio as well as investment opportunity identification.

The investment strategy will very closely resemble the flagship Magellan Global Fund. The portfolio will differ based on greater stock concentration (approximately an expected 20 versus the average 25 stocks in the Magellan Global Fund), less constrained risk parameters (largely to provide the additional flexibility possibly required for the more concentrated portfolio) and active currency hedging (the Magellan Global Fund is based on fully hedged and fully unhedged versions). The main difference however is around structure, being a closed-ended listed investment trust versus an open-ended unlisted managed fund or ETF.

MFG is bearing all the costs associated with establishing the listed vehicle and fund raising, which reflects very well upon MFG's strong commitment to the long term success of the Trust. This should ensure that the Trust's day one NAV is equal to the offer price as opposed to being at a discount (often the case).

Priority Offer

The Trust has a priority offer available to all existing Magellan Financial Group shareholders and/or registered unit holders of Magellan's active ETFs and unlisted managed funds as at 1st August 2017. As noted in the PDS, eligible investors can subscribe under the priority offer for the higher of either $30,000 equivalent to 20,000 units or $1 worth of units for every $10 directly or indirectly held in eligible vehicles. These investors will be eligible to receive a maximum number of additional loyalty units equivalent to 6.25% of the units received under the priority offer, subject to vesting conditions being met.

Eligible investors are subject to an escrow period. Specifically, to be eligible to receive the loyalty units these priority applicants are required to be unitholders in the Trust on 11 December 2017, but investors can trade the stock during the period from launch on 18 October 2017 until 11 December 2017 as long as they are on the register as at 11 December 2017. Any change in holding will be reduce the loyalty units accordingly.

MFG is effectively funding the priority offer from its own balance sheet and this will ensure that non eligible investors are not subsequently diluted and reflects a real concern of MFG that all investors are treated equitably. MFG will subscribe at the IPO for the number of loyalty units issued under the priority offer. After the vesting period, the Class A Units will be consolidated down by the number of Loyalty Units that are issued and will automatically convert to an equal number of ordinary units.

Distribution Policy

The Trust has a distribution policy of targeting a cash distribution yield of 4% p.a. which is to be paid semi-annually. The policy is designed to benefit investors both based on a relatively attractive level as well as the stability and predictability of what otherwise could well be quite a lumpy income stream. Target cash distributions will be based on an average monthly NAV over a two-year rolling period after the Trust has been in operation for two years. The Manager will set and telegraph the forecast distribution six months prior to payment date to provide certainty to investors. During the first two years from the Trust's inception date, the Manager intends to pay a $0.03 per unit distribution semi-annually, equating to a 4% p.a. yield based on the IPO price of $1.50 per unit.

The Trust will fund distributions from accrued income (realised capital gains/losses, dividend income, currency gains/losses) and potentially return of capital and cash holdings. The Magellan Global Fund has produced a distribution yield of 4.19% p.a. since inception.

However, this average figure is elevated on account of large distributions in 2015 (14.87%) and 2016 (8.13%). If these two years are excluded, the average is 2.44% p.a. Consequently, there is a risk of a shortfall, which if this transpires will have to be funded through the return of capital to unitholders by way of a proportional sell-down across the whole portfolio. The return of capital could be based on either, or a combination of, capital invested and / or past capital appreciation of the portfolio.

As a trust, MGG is a pass through vehicle in the sense that all income earned is distributed to investors in, effectively, the same period. Realised income will derive from realised capital gains / losses, dividend income from the underlying portfolio holdings, and foreign exchange gains / losses. Where realised income exceeds the 4% level, this additional amount will be paid to investors in the way of units in the Trust.

We note the Manager's point, specifically the mechanism is about efficiency. The Manager notes that investors preference is not to have inordinate amounts of the investment returned as a result of the crystallisation of large embedded capital gains caused by portfolio turnover. Having to pay this out in cash generally creates the need at the time of payment of distribution to sell positions to raise the cash for the distribution. This activity, in turn, crystallises more tax. By paying out as units, the Manager does not need to sell positions and therefore is not, unnecessarily, crystallising a tax obligations for investors.

We also note that the mechanism serves to grow NAV and, all things equal, reduces the risk that at any point in time disbutions, or a component of, is being funded from a return of capital invested.

Distribution Reinvestment Plan

The Manager has established a distribution reinvestment plan (DRP), which is expected to be a 5% discount to NAV. This discount will be funded by MFG, again ensuring an equitable outcome amongst all investors as there will be no subsequent dilution to investors who choose to not participate in the DRP.

Capital Management Initiatives

The Manager has also put in place several capital management initiatives to mitigate discount / premium to NAV risk. Specifically, the Manager has established a discretionary on-market buy-back program where units are trading materially below NAV.

Currency Hedging

The Manager has an active currency hedging investment mandate and will manage the Trust's currency exposures with the aims of generating positive total returns and, more importantly, to mitigate Australian dollar risk. The Fund can range from fully unhedged, partly hedged to fully hedged, depending on the Manager's currency views.

LIT vs LIC

MGG is based on a listed investment trust structure rather than a listed investment company structure – a LIT versus a LIC. The reason the Manager opted for the LIT structure was largely two-fold. Firstly, the Manager is of the view that the trust structure works better for distributions in that it gives the Manager the flexibility to lift cash distributions to 4% up front. In a company structure, distributions can only be paid out of the return of profits which take time to build up. Secondly, as a long term investor, generally when the Manager sells stocks the investment vehicle is beyond the CGT discount period of 12 months. Under a trust structure this CGT discount is passed through to the investor whereas this is not the case for those LICs that are income account (but is the case for those LICs on capital account).

Fees

The Fund has an annual management fee of 1.35% p.a. and a performance fee in which the Manager is entitled to 10% of net excess returns above the higher of either (a) the Australian 10-year Government Bond yield and (b) the MSCI World Net Total Return A$ Index and is subject to a high water mark. The dual performance benchmark is unusual but we view it as a positive, reflecting the Manager's focus on absolute returns rather than solely relative performance as well as it actually reducing the possibility of the Manager being eligible for the fee in any given period.

MANAGEMENT GROUP PROFILE

Magellan Asset Management (Magellan) was incorporated in July 2006 and is a fully owned subsidiary of the Magellan Financial Group (ASX Code: MFG). Magellan was co-founded by Chris Mackay (ex CEO UBS Australasia) and Hamish Douglass (ex co-Head Global Banking at Deutsche Bank). Founders, Directors and Staff own over 25% of the company.

The Magellan Global Fund and the Magellan Infrastructure Fund (Hedged) launched in July 2007 as unlisted registered managed investment schemes, with the wholesale Magellan Core Infrastructure Fund following in December 2009. In July 2013, Magellan launched a Global High Conviction strategy as well as providing investors with a hedged version of the Global Fund, and an unhedged version of the Infrastructure Fund.

Magellan has experienced rapid growth in FUM in recent years, with approximately $50 billion in total FUM as at 31 July 2017.

INVESTMENT TEAM

The Manager's investment team comprises 37 people, three of whom are dedicated traders and three dedicated members of the macro team. The analyst team is organised in six sector coverage teams (of five to seven members), covering different market sectors, namely, franchises, financials, technology and media, infrastructure, and healthcare. All members of the team cover stocks individually except for lead portfolio manager Hamish Douglass (the only person who doesn't directly cover any stocks). Historically, the Manager has experienced low levels of staff turnover, reflecting well on culture and morale and ensuring a consistency of investment process over time.

The Trust will be managed as a dual portfolio management structure with Stefan Marcionetti and Hamish Douglass as co portfolio managers. Stefan Marcionetti has been an assistant portfolio manager on the Magellan Global and High Conviction fund since 2016. Consequently, he is relatively inexperienced in this role but we are impressed by his knowledge and have conviction in his abilities to co-manage the portfolio.

The Manager's research process is overseen by Gerald Stack (Head of Investments) and Nikki Thomas (Head of Research). All key members of the investment team are held in high regard. While Hamish Douglass and Stefan Marcionetti have ultimate responsibility for portfolio construction, stocks are only eligible for inclusion if they have been approved by the 12-member Investment Committee. The Investment Committee is chaired by Gerald Stack and meets at least monthly.

The structure of the team is flat, collegiate and the Investment Committee structure ensures it is not overly dominated by any one individual. In terms of team size and use of resources, the team is very well resourced and also benefits from the use of external subject matter experts in certain fields. There is a strong alignment of interest between investment team and investors through a remuneration structure that is partly based on discretionary incentive programs and a staff Share Purchase Plan.

The qualifications and experience of key members of the investment team are summarised below, all of whom are also members of the Investment Committee.

Hamish Douglass, CEO, CIO and Co-Portfolio Manager. Hamish Douglass is Co-Founder, Chief Executive Officer and Chief Investment Officer of Magellan Financial Group, and Lead Portfolio Manager of Magellan's Global Equity strategies. Prior to Magellan, Hamish was Co-Head of Global Banking for Deutsche Bank AG in Australia and New Zealand. Hamish is a former member of the Australian Government's Financial Literacy Board, the Australian Government's Takeovers Panel, the Australian Government's Foreign Investment Review Board and the Forum of Young Global Leaders – World Economic Forum.

Stefan Marcionetti, Co-Portfolio Manager and Investment Analyst. Stefan Marcionetti joined Magellan in March 2013. Stefan is part of the Technology, Communications and Media team and in August 2016 was appointed to the additional role of Assistant Portfolio Manager. He was made a Portfolio Manager in 2017. Prior to Magellan, Stefan spent two and a half years as an analyst at Gladstone Partners, a London-based global fundamental long/short equity firm. Stefan also spent six years as an analyst in Deutsche Bank's Investment Banking team. Stefan holds a Bachelor of Commerce (First Class Honours) from the University of New South Wales.

Nikki Thomas, CFA, Head of Research and Portfolio Manager. Nikki Thomas joined Magellan in January 2007 with responsibility for research coverage of the Franchises sector. She took responsibility for managing the Franchises team soon thereafter and was promoted in 2011 to Portfolio Manager, a role in which she works closely with Lead Portfolio Manager, Hamish Douglass, on investment strategy and portfolio management of the Global Equity strategies. Nikki's role was expanded in December 2014 with her promotion to Head of Research. Prior to Magellan, Nikki spent 14 years in institutional stockbroking, holding equity analyst positions at BT Securities and at Deutsche Bank. Nikki has been a CFA Charterholder since 1997 and is an active member of the CFA Society of Sydney. She holds a Bachelor of Commerce from the University of New South Wales and is also a Chartered Accountant. Nikki is a member and Alternate Chair of Magellan's Investment Committee.

Gerald Stack, Head of Investments, Head of Infrastructure, Transport & Industrials, and Lead Portfolio Manager (Select Infrastructure). Gerald Stack joined Magellan in January 2007 and is Head of Investments, Head of Infrastructure, Transport & Industrials and Lead Portfolio Manager of Magellan's Select Infrastructure strategy. Prior to Magellan, Gerald was a Director of Capital Partners (now known as CP2) where he was Head of Securities Research and a member of the Management and Investment committees. Gerald holds a Bachelor of Economics and a Master of Business Administration, both from Sydney University, and is a Chartered Accountant. Gerald is Chair of Magellan's Investment Committee.

Domenico Giuliano, Deputy CIO and Portfolio Manager. Domenico Giuliano joined Magellan in March 2007 with responsibility for research coverage of the Financials sector. In 2011 Dom was promoted to Portfolio Manager, working closely with the CEO/CIO on investment strategy and portfolio management of the Global Equity strategies. In December 2014, Dom was promoted to Deputy Chief Investment Officer. Prior to Magellan, Dom spent 11 years in a variety of investment and actuarial roles. Dom holds a Master of Business Administration from the Australian Graduate School of Management and a Bachelor of Economics from Macquarie University, and is a Fellow of the Institute of Actuaries of Australia.

Key Investment Personnel

Name, Position	Years with Manager
Hamish Douglass, Co-founder, CIO, CO- Portfolio Manager	11 years
Stefan Marcionetti, Co-Portfolio Manager	4 years
Nikki Thomas, Head of Research	10 years
Gerald Stack, Head of Investments	10 years
Domenico Giuliano, Deputy CIO	10 years

INVESTMENT PROCESS

Broadly speaking, the investment process is well established, intuitively sensible, proven over the long term and clearly articulated by the Manager. There is a consistency of process, aided by the 12-member investment committee and, in this regard, we believe the track record of alpha generation and superior risk-adjusted returns over a full market cycle and the full range of market environments that has been recorded in the flagship Magellan Global Fund is very much repeatable.

Investment Philosophy

The core tenet of the Manager's investment philosophy is essentially that if you invest in high quality companies where there's much lower risk, and you buy at the right price, you should generate solid returns over the longer term and outperform the market.

The Manager also places a significant focus on capital preservation and mitigating downside risks. This is largely achieved through the qualitative assessment process tied with strong portfolio risk identification and management processes. When the Manager examines its portfolio in terms of the risks taken it is thinking very deeply about the actual individual businesses and the factor risks they are exposed to.

A key term the Manager uses when explaining its stock research process is "duration arbitrage". This means examining companies through a medium to long term lens and provides a different perspective on that business versus looking at it just in the short term (which the market often does). This provides various investment opportunities.

Investment Process

The Manager's investment process can be divided into three key 'legs' or processes; fundamental bottom-up stock research, broad and detailed macroeconomic research / insight, and rigorous portfolio construction and risk discipline.

Stock research is a purely qualitative process and commences with a very detailed initiation of coverage report, including valuation metrics. This is presented to a 12-member investment committee, comprising the most senior members of the investment team, to determine whether the company should be included on the approved investment list.

The assessment is based on four key qualitative criteria. Firstly, the Manager seeks to assess a company's economic moat, namely the sustainability of competitive advantage, or the sustainability of excess returns. The Manager is seeking to identify the underpinnings of a company's competitive advantage and to then think about the risks to these underpinnings. The Manager is making an assessment on the duration of a competitive advantage. If it's a business the Manager thinks has a very wide economic moat then it's a business that the Manager thinks can maintain its competitive advantage for decades into the future.

Secondly, business risk, which is the predictability of cash flow. Thirdly, Agency risk, which is whether management is doing the right thing in relation to matters such as compensation structures, acquisition history, etc. And finally what the Manager refers to as reinvestment potential, which is the growth potential and level of the incremental return. The investment committee will score each criteria to produce a total qualitative score for a business and consequently determine inclusion on the approved investment list of companies.

The approved investment list comprises around 200 companies at any point. The investment team closely monitors each constituent company on an ongoing basis.

We note that the voting process is democratic and egalitarian, with no individual having a casting vote or a greater weight than any other individual. The investment process therefore benefits from a plethora of different views and a conviction of broad judgement across multiple experienced individuals.

The second leg is macroeconomic insight. There are, in turn, two components of this. Firstly, as an opportunity identification source and, secondly, as a part of macro event risk identification in relation to portfolio holdings.

In relation to the first aspect, the Manager provided the example that in 2010 it took a view on the US housing market based on the very low levels of new housing sales and new home production as well as the renovation cycle being at a low point. The Manager formed a longer term view of the recovery and the improvement in the US housing market, and from that stemmed investments in home improvement retailers, Lowes and Home Depot. In this case, the macro insight led to an investment decision.

The second aspect, macro event risk identification, is however the more important component. What the Manager does here is seek to identify such risks in relation to each of its portfolio holdings and across the portfolio as a whole.

The third leg is portfolio construction and risk disciplines. The Manager's emphasis here is the identification of particular risks across the whole portfolio. Essentially a factor risk assessment process. Once identified and the factor risk aggregated across the portfolio, the Manager may then impose dynamic risk controls on the portfolio. Current examples include controls that the portfolio must not have more than 20% exposure in wholesale funding, 20% exposure in US housing, and 20% exposure to US interest rates. The Manager is only seeking to identify factor risks present in the portfolio and manage accordingly, rather than identify general broad market risks.

Additionally the Manager also has permanent portfolio risk controls, including but not limited to, maximum position sizes, minimum market capitalization, maximum cash position and minimum and maximum number of stock holdings.

The Manager's valuation process is based on two methodologies, specifically a longer-term DCF based assessment of a company's intrinsic value and a medium term measure based on a three year assessment of Total Shareholder Return (TSR). The DCF methodology is based on a three stage process; eight years of explicit forecasts, a 'horizon' period and a 'fade' period. This duration approach essentially reflects the economic moat of a company and the durability of a company's competitive advantage. The three-year TSR applies a forward price-to-earnings ratio to forecast earnings and forecast dividend yield is added to provide a forecasted three year return for a company.

Of the two measures, the medium term TSR has a greater weighting towards portfolio decisions, with the long term DCF serving more as a cross-check

Portfolio Construction

Portfolio construction is based on the fundamental processes described above and is overseen by the Investment Committee. Buy, sell and portfolio weighting decisions are the responsibility of Hamish Douglass and Stefan Marcionetti.

The Manager is seeking to construct the portfolio by including high quality companies that are trading at a material discount to valuation. To achieve this, the Manager utilises a Conviction Scoring Matrix which ranks each company on the approved investment list out of 100, with a 50% weight given to qualitative measures and 50% to valuation.

Sell decisions are driven by two factors; a change in the Manager's assessment of the quality of a business, specifically the outlook has materially diminished with the assessment of risk materially increasing, or secondly it has reached the Manager's valuation and on a relative risk/reward basis the company is no longer relatively attractive. That is, there are better companies to buy and hold on the approved investment list.

From a risk perspective, the Manager views the portfolio as comprising two halves; a low risk, defensive portfolio and a higher risk, shorter cycle portfolio through which the Manager will typically implement shorter cycle investment ideas. Holdings in the latter may have a lower quality score than those in the former, but compensated by a higher expected TSR.

The market sensitivity of the portfolio, effectively a beta measure, is allowed to be up to 1.0 compared to 0.8 in the Magellan Global Fund. This higher level has been set in the context of the more relatively concentrated nature of the Trust as well as the advantageous nature of a closed ended vehicle (not subject to investor inflows/outflows). Consequently, the Trust may have greater volatility than the Magellan Global Fund but, conversely, may reasonably be expected to have strong upside potential in strong equity market environments.

Portfolio turnover in the Magellan Global Fund has historically been relatively low at approximately 20% p.a. and is expected to be similarly so for the Trust. The average holding period in the fund is approximately thee to five years, with some stock holdings having been in the portfolio almost since inception. The relatively low turn-over and long term hold characteristic reflects the Manager's long-term lens on companies.

The currency exposure of the portfolio will be actively managed, with currency exposure based on underlying earnings of businesses / business units rather than simply domicile. A currency will not be hedged if the currency exposure accounts for less than 5% of the portfolio. Philosophically, the active currency management process is not about taking currency positions. Rather, it is about determining the appropriate level of hedging to remove Australian dollar risk.

The Manager has the ability to tactically allocate up to 50% of the portfolio to cash. As noted previously however, it would only be in the most extreme market environment that the Manager would contemplate approaching such a level. We note that during the height of the GFC, the Magellan Global Fund reached a maximum cash allocation of approximately 30%. The Manager views allocating to cash as not a risk free decision given the potential to underperform the market and, hence, places considerable emphasis on this assessment and decisions.

PERFORMANCE ANALYTICS

As noted, the Trust will be a very close cousin to the Manager's flagship Magellan Global Fund, albeit with several key differences. These differences, notably a slightly more concentrated portfolio and degree of risk plus active currency management, importantly do mean that the performance of the Trust will differ from the Magellan Global Fund moving forward. The point here is that the historic performance of the Magellan Global Fund may not be seen as a proxy for the Trust, rather, the intention in examining past performance is to assess investment skill, the ability to achieve stated investment objectives as well as assess the repeatability of investment process and hence alpha performance.

The Magellan Global Fund has been running since July 2007. The fund has recorded a net performance of 10.8% since inception, slightly exceeding the Manager's objective of 9% net returns after fees. We note that with this inception date the Manager has been tested in the full range of investment markets and over the full economic cycle. The fund has materially outperformed its benchmark, generating alpha of 6.0% p.a. since inception.

If we examine the 'shape' of MGF's performance over this period, the fund has generally materially outperformed in flat and negative market environments. The funds outperformance over the 2008 was marked, especially in 2008 and 2011. In strong up markets, the fund has generally been in-line with market performance, which has broadly been the case from 2013 to 2017 YTD. Reflecting this, up market capture, the extent to which relative performance tracks the benchmark, has been consistently around 1.0 since inception. However, down market capture is around 0.6 since inception, recording materially lower drawdowns during those periods in which the market was recording significant falls. This is very much by design and consistent with the Manager's strong focus on capital preservation.

From a risk perspective (standard deviation), MGF has generally recorded volatility in line with the market (not unexpected given a concentrated portfolio). Downside volatility has been slightly less though, reflecting well on the Manager. Key risk/return measures (Sharpe Ratio and Sortino Ratio) are materially higher since inception and generally in-line during positive market environments.

Magellan Global Fund (unhedged) as at 31 August 2017

	1-year	3-year	5-year	7-year	Since Inception
Magellan Global Fund	10.04%	13.92%	17.48%	15.94%	10.83%
MSCI World Index	10.09%	11.90%	17.14%	12.99%	4.85%
Out/Under Performance	- 0.05%	2.01%	0.34%	2.95%	5.98%

PEER COMPARISON

- We have compared MGG to six LICs listed on the ASX that provide exposure to a portfolio of global equities. The Trust has yet to list so we have provided a comparison of some of the key features of the peer group, namely fees and dividend yield.
- The Trust's annual management fee is the highest of the peer group. However, this is partly offset by the performance fee rate being lower than the majority and with, in our view, a superior dual hurdle structure. We note that there is one LIC in the group that does not have a performance fee.
- Historic dividend yields vary materially across the peer group but are generally below that of domestic equities as can reasonably be expected. Not surprisingly given the Trust's distribution structure, the Trust is expected to sit at the higher end of the peer group. Investors should note however that the comparison is not strictly like-for-like given the return of capital component of the Trust's cash distribution and the fact that LIC dividends can be franked.

Peer Comparison

LIC / LIT Name	ASX Code	Management Fee (%p.a, ex GST)	Performance Fee (%)	Div Yield (%)*	Performance Fee Hurdle
MFF Capital Investments **	MFF	0.42%	**	1.00%	TSR above 10%
Platinum Capital	PMC	1.10%	15%	4.50%	MSCI All Country World Net Index
Templeton Global Growth	TGG	1.00%	None	3.30%	n.a.
Hunter Hall Global Value ***	HHV	1.20%	15%	6.00%	MSCI World TR Index AUD
Contango Global Growth ****	CQG	1.25%	10%	n.a.	MSCI ACWI ex Australia (AUD)
Ellerston Global Investments	EGI	0.75%	15%	2.00%	MSCI World Index (local)
Magellan Global Trust	MGG	1.35%	10%	4.00%	MSCI World Net TR Index AUD / Aust 10-year Govt Bond Yield

* Dividend yield is based on last 12 months dividends to 31 July 2017. MGG yield is target cash distribution yield.

** Flat fee of $4m p.a. plus potential performance fee of $1m

*** Proposal to reduce base fee from 1.5% to 1.2% to be put to 2017 AGM.

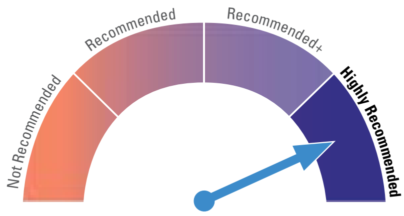
**** The maximum performance fee payable in any financial year will be capped at 0.75% of the value of the portfolio. Any amount due above this will be carried forward to future financial years and can be offset against periods of underperformance.

APPENDIX A – RATINGS PROCESS

INDEPENDENT INVESTMENT RESEARCH PTY LTD "IIR" RATING SYSTEM.

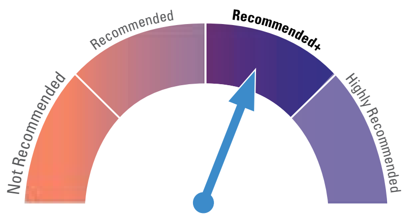
IIR has developed a framework for rating investment product offerings in Australia. Our review process gives consideration to a broad number of qualitative and quantitative factors. Essentially, the evaluation process includes the following key factors: product management and underlying portfolio construction; investment management, product structure, risk management, experience and performance; fees, risks and likely outcomes.

Highly Recommended	**83 and above**



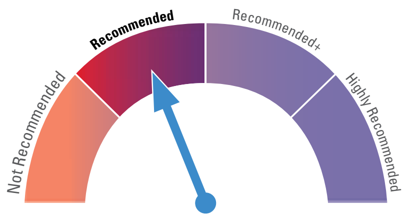
This is the highest rating provided by IIR, indicating this is a best of breed product that has exceeded the requirements of our review process across a number of key evaluation parameters and achieved exceptionally high scores in a number of categories. The product provides a highly attractive risk/return trade-off. The Fund is likely effectively to apply industry best practice to manage endogenous risk factors, and, to the extent that it can, exogenous risk factors.

Recommended +	**79–82**



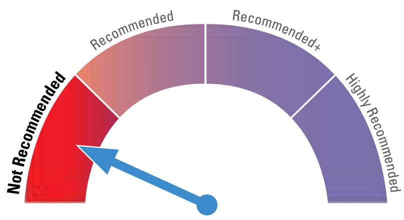
This rating indicates that IIR believes this is a superior grade product that has exceeded the requirements of our review process across a number of key evaluation parameters and achieved high scores in a number of categories. In addition, the product rates highly on one or two attributes in our key criteria. It has an above-average risk/return trade-off and should be able consistently to generate above average risk-adjusted returns in line with stated investment objectives. The Fund should be in a position effectively to manage endogenous risk factors, and, to the extent that it can, exogenous risk factors. This should result in returns that reflect the expected level of risk.

Recommended	**60–78**



This rating indicates that IIR believes this is an above-average grade product that has exceeded the minimum requirements of our review process across a number of key evaluation parameters. It has an above-average risk/return trade-off and should be able to consistently generate above-average risk adjusted returns in line with stated investment objectives.

Not Recommended	**<60**

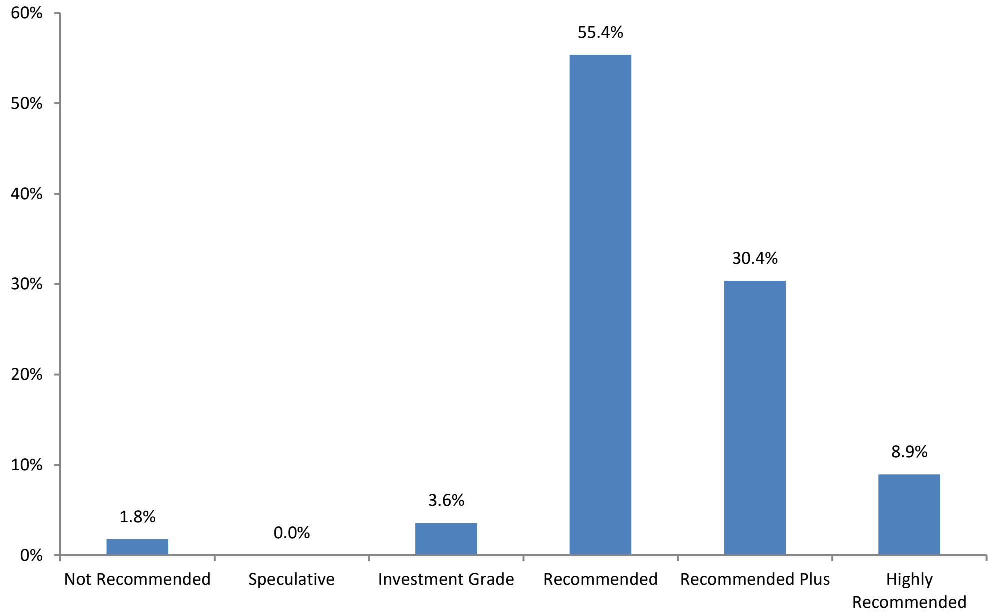


This rating indicates that IIR believes that despite the product's merits and attributes, it has failed to meet the minimum aggregate requirements of our review process across a number of key evaluation parameters. While this is a product below the minimum rating to be considered Investment Grade, this does not mean the product is without merit. Funds in this category are considered to be susceptible to high risks that are not reflected by the projected return. Performance volatility, particularly on the down-side, is likely.

APPENDIX B – MANAGED INVESTMENTS COVERAGE

The below graphic details the spread of ratings for managed investments rated by Independent Investment Research (IIR). The managed investments represented below include listed and unlisted managed funds, fund of funds, exchange traded funds and model portfolios.

SPREAD OF MANAGED INVESTMENT RATINGS



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