VGI
PARTNERS

30 July 2019

Investor Letter

"More money has been lost by chasing yield than at gunpoint"

- Wall Street aphorism often attributed to John D. Rockefeller

Dear Fellow Investors,

For the twelve months ended 30 June 2019 (FY19), **VGI Partners Global Investments Limited** (ASX: **VG1**) generated a post-tax net return of +10.2% after all fees.

VG1's average monthly gross exposure in FY19 was 99% (74% long investments plus 25% short positions), with an average monthly net exposure of 49%. This means that on average for every $100,000 you had invested in VG1 during FY19 we owned $74,000 of equities and sold short $25,000 of equities for a net equity exposure of $49,000.

We set out the above as we believe it is critical for our investors to recognise that VG1's recent returns have been generated with a substantial cash buffer. This provides VG1 with significant purchasing power to buy high-quality companies at prices that meet our valuation criteria when market volatility inevitably reappears.

VGI Partners' investment process and philosophy is based firmly on the cornerstone principles of capital preservation and 'margin of safety'. We are extremely focused on avoiding any permanent loss of capital.

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We aim to increase the likelihood of capital preservation primarily through two means. First, by investing in high-quality businesses that are easy to understand and that trade at prices which we believe exhibit a sufficient margin of safety – that is, trading at prices that are significantly below the intrinsic value of the business. And second, by using little or no leverage and keeping prudent cash buffers.

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As long-term VGI investors know, we like to begin our investor letters with an instructive quote that reflects our thinking at the time of writing. We decided to begin this letter with the observation attributed to John D. Rockefeller: ***"More money has been lost by chasing yield than at gunpoint."***

Rockefeller's remark is top of mind at present as global government bond yields have continued their steady decline in recent months.

In an increasing number of countries, governments are now borrowing at negative yields. Negative-yielding government debt reached US$13 trillion in June 2019, having almost doubled since December 2018, and now makes up around 20% of global government debt. German 10-year government bonds are currently yielding -0.3%, meaning investors are paying to hold these instruments rather than receiving interest. To reiterate: investors are actually paying the German government €3,000 annually for every €1,000,000 the government wants to borrow over 10 years. Similarly, investors are willing to pay 0.1% per annum to hold Japanese 10-year government bonds. This is an unprecedented environment to say the least!

In another extreme example, last month Bolivia issued a 50-year government bond, denominated in Bolivian Boliviano, at a rate of just 4.1%. Since 1980 alone, Bolivia has defaulted on its debts three times.

Lower global risk-free rates translate to lower yields on bonds which in turn means lower incomes for fixed interest investors. Falling yields force many investors to take higher risk, sometimes without even realising it, in an effort to maintain their income.

It is no surprise that this quest to maintain income levels has been met by large global fund managers via a plethora of new financial “products” claiming to all but guarantee significantly better-than-cash returns (sometimes even promising monthly distributions). Many of these products neglect to properly outline to would-be investors the longer-term capital risks of such strategies. Some of these products go so far as to pay investors their capital back in installments while dressing it up as an income stream.

What Rockefeller meant is that this incessant chase for yield can mean that investors ignore the risks they are taking with their capital in an effort to generate more income. Rarely does this end well.

These riskier investments tend to perform to plan during favourable market conditions, when investors are less focussed on potential downside. However, this can change very quickly. We saw this in 2008, for example, when the Barclays Global High Yield Bond Index fell by 27%!

While conditions are currently benign, there is a time in every market cycle when Mark Twain’s famous quip reflects the thoughts of every investor who, with hindsight regrets reaching a little too far for yield - ***“I am more concerned about the return of my money than the return on my money”***.

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Due in large part to the low interest rate environment that we discuss above, we find that the vast majority of high-quality businesses continue to trade at valuations which imply unlikely levels of growth into perpetuity, combined with an expectation that interest rates will remain low forever. While this is a scenario which can hold for some time, these are assumptions we simply do not feel comfortable making. One thing we will not do is lower our quality or valuation thresholds in order to justify an investment for the sake of being more fully invested. As a result, we continue to maintain a relatively sizable cash holding which enhances our ability to execute in times of market uncertainty.

While valuations remain elevated across the globe, we have been finding more opportunities in the Asian region. Asian businesses have become more prominent both in the portfolio and on the VGI Partners "wish list" than has generally been the case in the past. This is due to a confluence of factors. For several years, we have been monitoring meaningful improvements in corporate governance standards in parts of developed Asia. In addition, we have seen signs that many high-quality companies are becoming more investor friendly, particularly regarding capital management initiatives. Increased shareholder activism across the region, and particularly in Japan, has played a part in this development.

This has prompted us to spend more of our time and energy focused on opportunities in Asia, including establishing a Tokyo research office a little over a year ago. VGI Partners' Tokyo office now accommodates four members of our Investment Team, with skills in a range of Asian languages. We have opened this office at a time when the representation of international investors in Japan is in decline. With the region now under-researched it is no surprise that we have been able to identify a number of extremely high-quality businesses trading at attractive valuations.

As always, we remain confident that we will continue to generate superior risk-adjusted returns <u>over the long- term and through investment cycles</u> by concentrating our capital in a relatively small number of high-quality businesses that we believe are significantly undervalued and by avoiding the use of leverage.

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Two inter-related initiatives were completed during FY19 that enhance VG1's longer-term position and further align the interest of VG1 investors with those of VGI Partners, the Manager of VG1.

The first of these initiatives was a $300 million equity raising ("VG1 equity raising") which completed in June 2019, comprising:

- A $98 million placement (41.8 million VG1 shares) to existing investors in unlisted funds managed by VGI Partners; and
- A $202 million, 1-for-3.22 pro rata renounceable entitlement offer (86.5 million VG1 shares) to existing VG1 shareholders. The offer was strongly supported and was ultimately oversubscribed by approximately 15%.

All VG1 shares were issued at $2.34 per share (the NTA at 30 April 2019, which represented a 5% discount to the last closing price at the time of announcement). All raising costs were borne by VGI Partners, and not VG1.

With the VG1 equity raising having completed in the second half of June, VG1 finished the period with a relatively high cash weighting. This provides considerable flexibility for future deployment, while VG1's expanded capital base will provide additional liquidity for investors in the company.

The second initiative was the initial public offering of VGI Partners ("Manager IPO"). We made a very deliberate decision to make the opportunity to participate in the Manager IPO available exclusively to participants in the VG1 equity raising. By doing this, we were able to make the Manager IPO an important new alignment initiative, providing VG1 investors with the opportunity to benefit, as owners, from VGI Partners' future growth and success. Reflecting this objective, the Manager IPO was deliberately priced at a level we expected VG1 shareholders would find attractive.

In light of the above, it is extremely pleasing to report that VGI Partners shares have traded strongly subsequent to listing on 21 June 2019. Shares closed at $12.50 on 29 July 2019, up 127% from the $5.50 listing price.

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VG1's **+10.2%** net return for FY19 consisted of stock contribution totalling **+6.9%** and a contribution from our long-term strategic currency positioning of **+3.3%**. We will discuss our active currency management approach in detail later in this letter.

When the VG1 Prospectus was prepared in 2017, we outlined the expectation that VG1 would replicate the proven and successful VGI Partners Master Fund portfolio over time. Given the relatively short performance period available for VG1 since inception, we believe that it is useful to include the following table showing the net returns of the VGI Partners Master Fund.

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The following table shows the returns of the VGI Partners Master Fund, which is Australian Dollar (**AUD**) denominated, **after all applicable fees and charges**.

Year to 30 June	VGI Partners	Index*	Relative	VGI Partners Net Exposure
2009 (6 months)	2.3%	(3.4%)	5.7%	15%
2010	8.3%	5.1%	3.2%	76%
2011	18.4%	3.2%	15.2%	88%
2012	5.4%	(0.6%)	6.0%	71%
2013	27.5%	33.1%	(5.6%)	77%
2014	9.4%	20.1%	(10.7%)	86%
2015	38.1%	24.0%	14.1%	76%
2016	13.0%	0.6%	12.4%	75%
2017	5.9%	14.6%	(8.7%)	58%
2018	20.2%	15.4%	4.8%	54%
2019	13.1%	12.1%	1.0%	62%
Total Return Since Inception	**332.9%**	**208.1%**	**124.8%**	**70%**
Compound Annual Return	**15.0%**	**11.3%**		

Source: Citco Fund Administration and Bloomberg.
Performance is shown after all applicable management and performance fees charged.
* Index = MSCI World Total Return Index (AUD). The MSCI Index is 100% net invested at all times.

Since inception in 2009, our Fund has generated a net return of **+332.9%** after all fees, compared to the return of the MSCI World Total Return Index (AUD) of **+208.1%** over the same period. This represents total outperformance versus the MSCI World Total Return Index (AUD) of **+124.8%** since inception and a compound annual net return to investors of **+15.0%** over this period.

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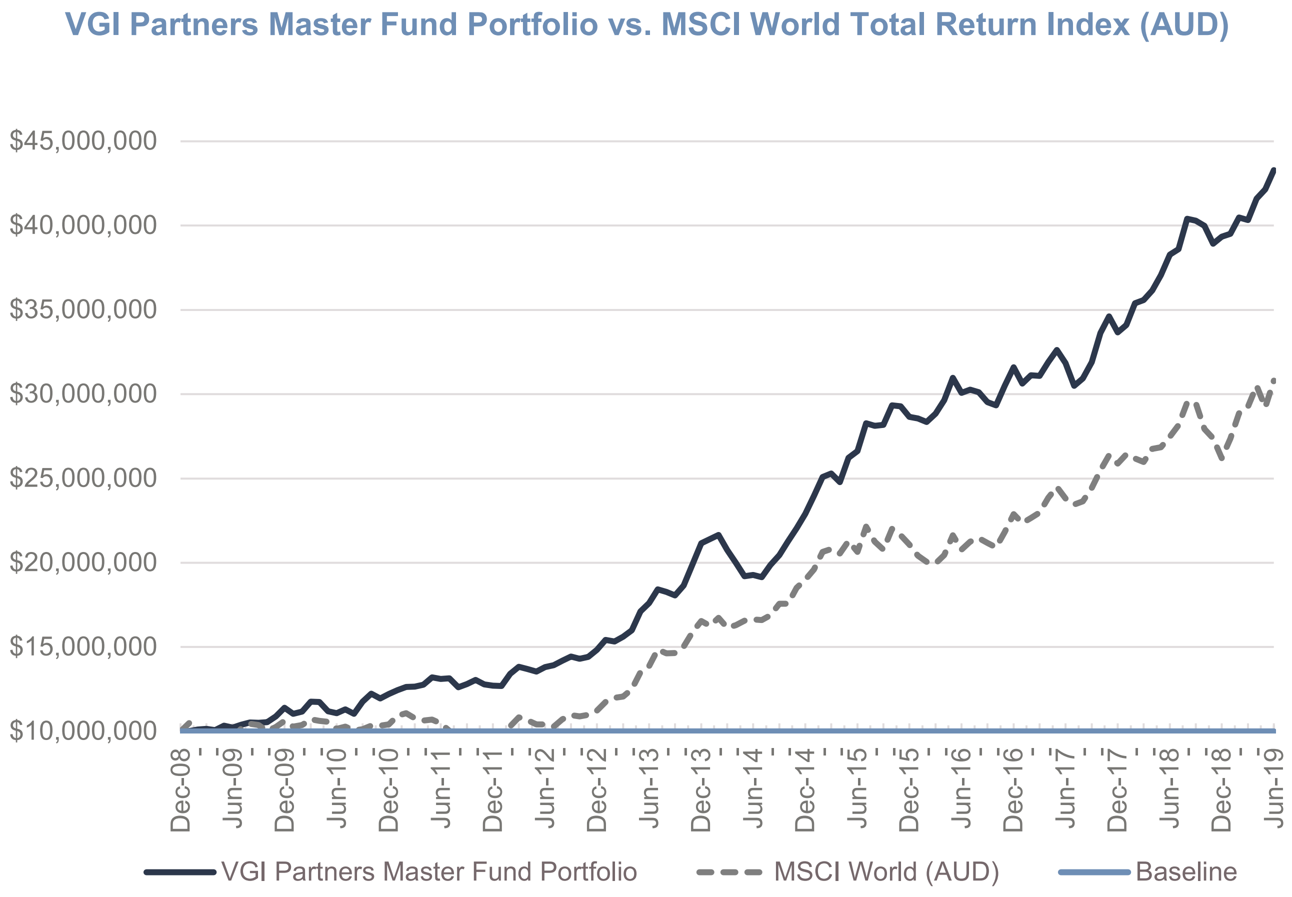
The VGI Partners Master Fund's performance since inception is shown graphically in the below chart compared to the MSCI World Total Return Index (AUD):



Source: Citco Fund Administration and Bloomberg.

As you can see, the VGI Partners Master Fund has outperformed the Index (which is 100% invested and thus holds 0% cash) over time despite the Portfolio holding an average cash weight of 30%. We believe that this is a practical way to illustrate VGI Partners' ability to deliver a risk-adjusted return over time.

We believe the charts overleaf are an intuitive way to demonstrate VGI Partners' strong focus on capital preservation and our conservative portfolio positioning. Over the past eleven years, the portfolio has delivered compound annual returns of 15.0% after all fees. This compares to 11.3% for the Index. The chart on the right-hand side shows that since inception, the VGI Portfolio has tended to outperform in periods of market weakness. The VGI Portfolio fell an average of just -0.7% in down market months, when the Index fell by -2.3% on average.

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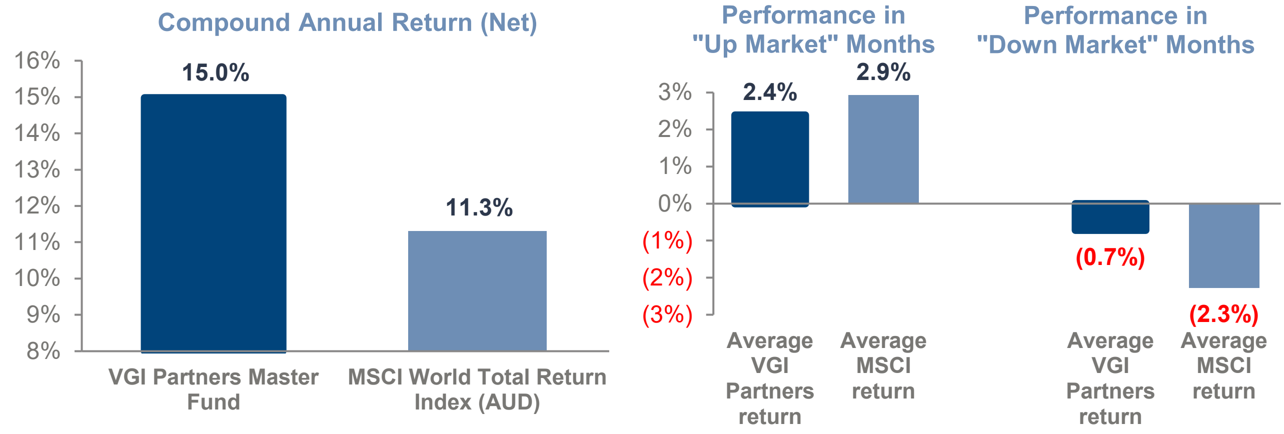
Performance and Capital Preservation in Up / Down Months



Source: Citco Fund Administration and Bloomberg.
Note: The performance period includes 126 months since inception (78 "up market" months and 48 "down market" months).
MSCI = MSCI World Total Return Index (AUD).

Our investment philosophy of concentrating capital in our best ideas, complemented by selective short selling and holding strategic cash reserves when valuations are not attractive, has been effective over the past eleven years. We remain highly disciplined and focussed on ensuring our process is adhered to at all times. We will not change our process to chase a bull market in a 'hot' sector or region, or to chase yield as discussed earlier.

Looking to the future, we believe that consistent application of our investment process, coupled with ongoing scepticism and hard work by our highly focussed Investment Team will deliver superior risk-adjusted returns on our collective capital over a multi-year period.

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Performance Attribution for the Year to 30 June 2019

The following table lists the most significant stock contributors to the performance of VG1's Long Portfolio for the twelve months to 30 June 2019.

Top Long Contributors to Returns in FY19	Contribution
CME Group Inc.	2.4%
MasterCard Inc.	2.2%
Amazon.com Inc.	1.5%
Linde plc	1.3%
Medibank Private Ltd.	1.3%
Colgate-Palmolive Co	1.1%
Total Contribution of Above	**9.8%**

Source: VGI Partners.

CME Group (NASDAQ: CME) is currently VG1's largest investment with a **9.5%** weighting. CME contributed **+2.4%** to performance for the twelve months to 30 June 2019, with the share price increasing **18.4%** over the course of the year. In addition, CME paid us five dividends totalling $4.65 per share, for a dividend yield of **2.4%**.

CME is a derivatives exchange with an effective monopoly in the exchange trading of US interest rate derivatives and a dominant position in the trading of global commodities, foreign exchange, equity index and energy derivatives.

We believe that CME's interest rate volumes (which contribute approximately 30% of the company's revenues) are likely to substantially increase when interest rate volatility returns. Recent volumes remain robust despite a fairly benign interest rate outlook. Furthermore, we believe the business model is extremely well-positioned for any pick-up in inflation.

CME has consistently demonstrated shareholder-friendly capital allocation policies, returning excess cash to shareholders in the form of increased dividends and share buybacks.

MasterCard (NYSE: MA) contributed **+2.2%** to performance for the twelve months to 30 June 2019, with the share price increasing **34.6%** over the course of the year.

MasterCard is the world's second largest global payments processor, behind Visa. The industry is a duopoly with MasterCard and Visa controlling the majority of the world's electronic payments. We believe that a strong secular trend toward electronic payments over cash and cheques will continue to drive both the revenue and earnings of MasterCard. Significant growth opportunities exist in developing countries as well as in new payment technologies (such as PayPass) that enable the more frequent use of electronic payments. We also view MasterCard as an attractive hedge against inflation – a higher cost of goods purchased will benefit the company's bottom line as it charges an ad valorem fee and has significant pricing power.

At the time of MasterCard's IPO in 2006, 85% of the world's consumer payments by value were transacted in cash. Today, despite the widespread adoption of electronic payments in developed markets, the global share of cash transactions still stands at 85%. This has occurred as emerging market transaction growth has outpaced that of developed markets. In emerging markets, 92% of transactions are still carried out in cash. This dynamic provides MasterCard with an incredibly long runway of growth.

On top of the secular tailwinds, attractive industry structure and inflation protection, MasterCard also has a high-quality management team that has maintained a debt-free balance sheet despite investing heavily in future growth projects.

Amazon.com (NASDAQ: AMZN) contributed **+1.5%** to performance for the twelve months to 30 June 2019, with the share price increasing **11.4%** over the course of the year. We believe that Amazon has built a non-replicable global logistics network, providing it with a very wide and expanding economic moat in the rapidly growing online retail space. Incredibly, Amazon has built this business over the past twenty five years without raising material equity or net debt. This shows us that Amazon has been able to fund its growth through a highly cash generative core business. We remain confident that Amazon's retail and logistics business will enjoy many years of impressive revenue growth and margin expansion.

In addition, Amazon is the leading global cloud computing provider through Amazon Web Services (AWS). This fast-growing market was effectively founded by Amazon, and as a result AWS benefits from significant first-mover and scale advantages. Amazon is also rapidly growing its advertising business, another additional source of high-margin revenues.

Amazon is a core position for us and while we do expect there to be significant share price volatility from time to time, as we have seen at times in the past, we expect that over the long-term we will continue to generate strong returns on our investment.

Linde plc (NYSE: LIN) contributed **+1.3%** to performance for the twelve months to 30 June 2019, with the share price increasing **27.0%** over the course of the year.

Linde plc is the result of a merger between two of the big four industrial gas providers, Praxair Inc. and Linde AG. The merger closed in March 2019 and the combined business, Linde plc, is now the largest industrial gas player in the world, further consolidating an already highly concentrated industrial gas industry.

We believe a number of factors make the industrial gas industry an attractive investment. The product is a fraction of their customers' total cost base but an essential input, providing substantial pricing power. Industrial gas facilities require substantial initial capital requirements and often it will take three years to see any return on this investment. The industry has very long-term contracts with 'Take or Pay' provisions, improving earnings visibility. In addition, the industry has a highly consolidated market structure, with the top three players holding ~80% of the global market. Finally, the industry tends to form regional monopolies, as production must occur within 200km of the end customer.

We have been Praxair shareholders for many years as, in addition to the above factors, Praxair has a very high-quality, long term focused management team who are aligned with shareholders as a result of their substantial shareholding.

This Praxair management team is, as of March, in control of the merged business and we believe their best-in-class execution combined with Linde AG's assets will result in significant pricing opportunities and margin improvement over the coming years.

Medibank Private (ASX: MPL) contributed **+1.3%** to performance for the twelve months to 30 June 2019, with the share price increasing **13.3%** over the course of the year, with a fully franked dividend yield of **5.3%** on top.

Medibank's recent share price performance has largely been driven by the re-election of the Coalition government. The Australian Labor Party had threatened to cap Private Health Insurance premium increases at 2% per annum for two years if elected, which would have been a short-term headwind for the industry.

Medibank is Australia's largest private health insurer, with 26% market share. There are several characteristics that we like about the Australian Private Health Insurance sector, including an aging population, Federal Government tax incentives to take up Private Health Insurance and a renewed focus on eliminating waste from the healthcare system.

Medibank was publicly listed on the ASX by the Australian Government in late 2014 after 37 years of government ownership. We take notice when there is a public offering of a unique asset owned by a developed world government. More often than not, we find that these companies can be run far more efficiently in private hands than under state ownership. This has certainly been the case with Medibank.

When Medibank was listed on the ASX, the Medibank Private Sale Act prohibited any single investor from owning more than 15% of the company, thus prohibiting a takeover. This restriction expires in November 2019 and we believe there are several potential bidders that would covet the market share that Medibank has in the Australian Private Health Insurance industry.

Further, Australia's prudential regulator is encouraging consolidation of the Private Health Insurance industry. As the largest player, we believe that Medibank is best positioned to benefit from this over the long run.

Colgate-Palmolive Company (NYSE: CL): Colgate contributed **+1.1%** to performance for the twelve months to 30 June 2019, with the share price increasing **10.6%** over the course of the year. In addition, Colgate paid us dividends of $1.69, for a dividend yield of **2.4%**.

Founded in 1806 in New York City by William Colgate as a soap and candle business, Colgate-Palmolive has grown into one of the world's largest consumer products companies.

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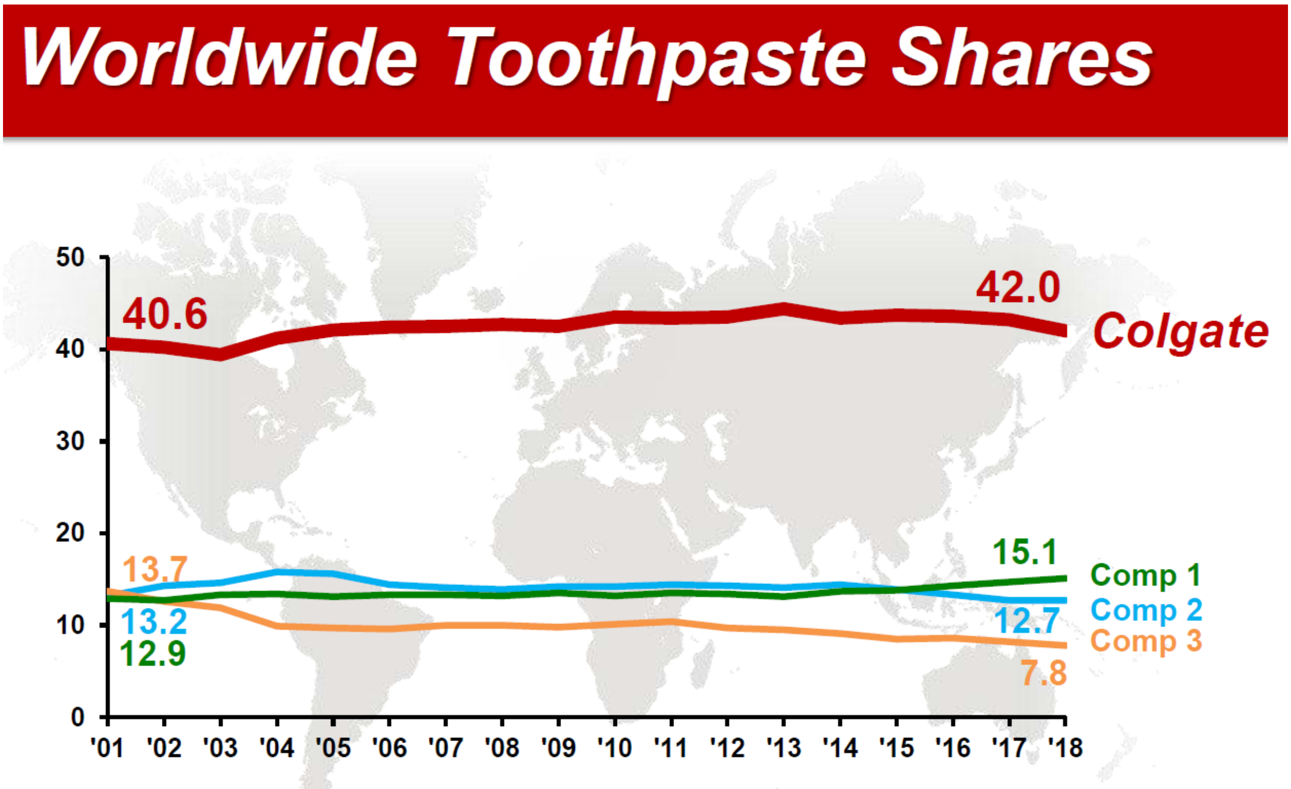
Colgate has a large international exposure with 70% of its revenue generated from outside the US, including 50% from high growth emerging markets. Colgate's global market share of toothpaste is a staggering 42%, up from 35% in 1995. The below chart also shows that Colgate's global market share today is almost three times its nearest competitor. The brand's share of some of the largest emerging markets is even higher, with Brazil at 72% and India at 50%.



Source: Colgate Investor Presentation February 2019.

Colgate's high share of the toothpaste market in these geographies owes a great deal to the company's decision to set up distribution early, providing a first-mover advantage. Market shares in toothpaste are generally quite stable as consumers show strong loyalty to the brand of toothpaste they grew up with. We believe Colgate's emerging market exposure is a significant positive over the long-term as growth in population and disposable income outpaces that of developed markets.

Colgate follows a strategy of long term premiumisation. Once it has established a leading market position, it slowly but steadily introduces superior products at a higher price point and gross margin. This progression is almost too slow to be noticed by customers but over many years has led to significant gross margin expansion for the business. Remember the original plain red tube of Colgate toothpaste that contained no teeth whitening, mint stripes or sensitive pain relief? You can still buy this at the local supermarket at a relatively low price, however Colgate has most likely traded you up to one of their more expensive products.

In addition to oral care products, Colgate owns the Hill's Pet Nutrition business which is a global leader in specialty pet foods and sells under the Hill's Science Diet™ and Hill's Prescription Diet™ brands among others. If you have a dog or cat at home, you may recognise these as brands that vets recommend - vets are to pet food today what dentists were to toothpaste 40 years ago. This is a terrific business that benefits from the secular trend of higher pet ownership and greater expenditure on 'companion animals' in developed markets.

Colgate generates extraordinary returns on both equity and capital without the use of any material leverage. It has one of the highest tax rates of its peers, which we expect to come down over time. Colgate is also one of the most consistent dividend paying stocks globally. In fact, Colgate has paid an uninterrupted dividend since 1895, even throughout the Great Depression; that's 124 years of consecutive dividends. On top of this it has increased its annual dividend payment in each of the past 56 years. This is our kind of business!

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In this section of our letter we usually set out any individual positions that detracted from the performance of our Long Portfolio by more than 1.0% over the last twelve months. We do this in an endeavour to learn from our mistakes and not make the same ones in the future.

Over the past twelve months we have only had one long position that detracted more than 1.0%.

Zillow Group (NASDAQ: Z) detracted **-1.6%** from performance for the twelve months to 30 June 2019, with the share price decreasing **-21.5%** over the course of the year. Zillow operates the leading residential real estate marketplace websites in the US. We were originally attracted to this business as we saw a shift of real estate advertising dollars towards online platforms and, as the dominant player, Zillow was positioned to be the main beneficiary of this trend.

We were attracted to the core advertising business as it is highly profitable, has limited competition and requires very little capital investment. However, in early 2018 Zillow announced they would move into buying and selling homes directly. We were immediately sceptical regarding this new business of buying and selling homes as it is highly competitive, operates with razor-thin margins and requires significant capital investment to grow (as the cost of each house is significant).

While it was initially unclear whether the home-flipping business would be a small-scale experiment or a more substantial shift in corporate strategy, we started to reduce our exposure to Zillow shortly after the move into home-flipping was announced.

It is now apparent that Management is committed to significantly accelerating the buying and selling of homes across the US. Zillow will use financial leverage to grow this business which gives rise to a new potential risk to the balance sheet in the event of a housing downturn. As a result of this significant change in business model, we have exited our Zillow investment.

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Short Portfolio

Collectively, our short portfolio contributed **+0.7%** to performance in FY19. The short portfolio averaged 25% of total portfolio capital throughout FY19 and decreased in value by 2.6%. That is to say that on a weighted average basis the stocks that we were short throughout the year decreased in price by 2.6%, which compares to an increase of 12.1% in the MSCI World Total Return Index (AUD). Consequently, our short positions improved our overall net returns by 0.7% in FY19.

With reference again to the VGI Partners Master Fund (as it has a longer track record), over the past five years, our short portfolio has contributed **+3.0%** to returns (meaning that on average the stocks we have shorted have fallen in price). This has been achieved in a period when the MSCI World Total Return Index (AUD) increased by 85.1%. The fact that we have generated positive returns from our short portfolio over this period of rising equity markets demonstrates our ability to short-sell securities profitably over the long run.

Over time we believe our short positions, which are focussed on structurally flawed businesses, fads and accounting irregularities, will continue to generate positive returns for VG1.

An added benefit of looking for potential short candidates is that everyone on the VGI Partners Investment Team is constantly on the lookout for what we call 'red flags'. Red flags can come in many forms, including key insiders selling stock, accounting issues or the competitive landscape of an industry shifting. The VGI Partners Investment Team analyses this data with a sceptical eye, a key skill which we believe adds value to our analysis of the long portfolio by helping us identify early any emerging red flags in our long investments.

Finally, and importantly, these short positions also enable us to reduce market exposures and profit from falling equity markets during periods of uncertainty and heightened volatility. This provides us with a very valuable tool with which we can cushion VG1's returns during a downward trending market.

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Portfolio Update and Current Positioning

The following table details our current Top 5 long investments and clearly demonstrates that we continue to concentrate VG1's capital in our best ideas. Today, our Top 5 long investments represent 35% of total portfolio value. We do not diversify for diversification's sake – we believe that carefully concentrating investments remains the best strategy for preserving and growing our collective capital.

Top 5 Long Investments	% of Fund
1. CME Group Inc.	10%
2. Amazon.com Inc.	7%
3. Spotify Technology	6%
4. Colgate-Palmolive Co	6%
5. MasterCard Inc.	6%
Total	**35%**

Source: VGI Partners.

Our Long Portfolio is complemented by a forensically selected group of stocks we have sold short. The combination of the two, over time, works in unison to reduce equity market exposure while at the same time contributing to our portfolio returns.

VG1 currently has 52% net equity exposure, with 72% long and 20% short.

We mentioned earlier in this letter that a number of the high-quality businesses that we follow, and would like to own, are currently trading at valuations that we are not comfortable with. Nonetheless short term volatility sometimes provides us with opportunities and in FY19 we added three new long positions to the portfolio.

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Alignment of Interests

As we have discussed in previous letters, we take alignment of interest between ourselves and you, our valued Investment Partners, very seriously.

VGI Partners' investment staff have the vast proportion of their net worth invested in our two Funds, VG1 and VGI Partners itself. All staff are prohibited from purchasing securities outside the Funds, VG1 and VGI Partners. We subscribe to the view that a manager should eat his or her own cooking and at VGI Partners that's exactly what we do. As a result, we and our families and close friends are the first ones to know if the cooking is not up to scratch!

"In the building practices of ancient Rome, when scaffolding was removed from a completed Roman arch, the Roman engineer who built the arch stood beneath. If the arch came crashing down, he was the first to know! His concern for the quality of the arch was intensely personal, and it is not surprising that so many Roman arches have survived."

- Seth Klarman, 'Margin of Safety'

Over the past eleven years, all members of the VGI Partners Investment Team have consistently added to their investment in the Funds managed by VGI Partners. We all view these investments as our primary capital growth vehicle and thus our most important financial investment.

As a result of the above, you should be confident that our Investment Team's energy and effort is focussed on a singular outcome – to maximize returns while preserving capital for our collective Portfolio.

At VGI Partners we focus all of our time and energy on managing your money.

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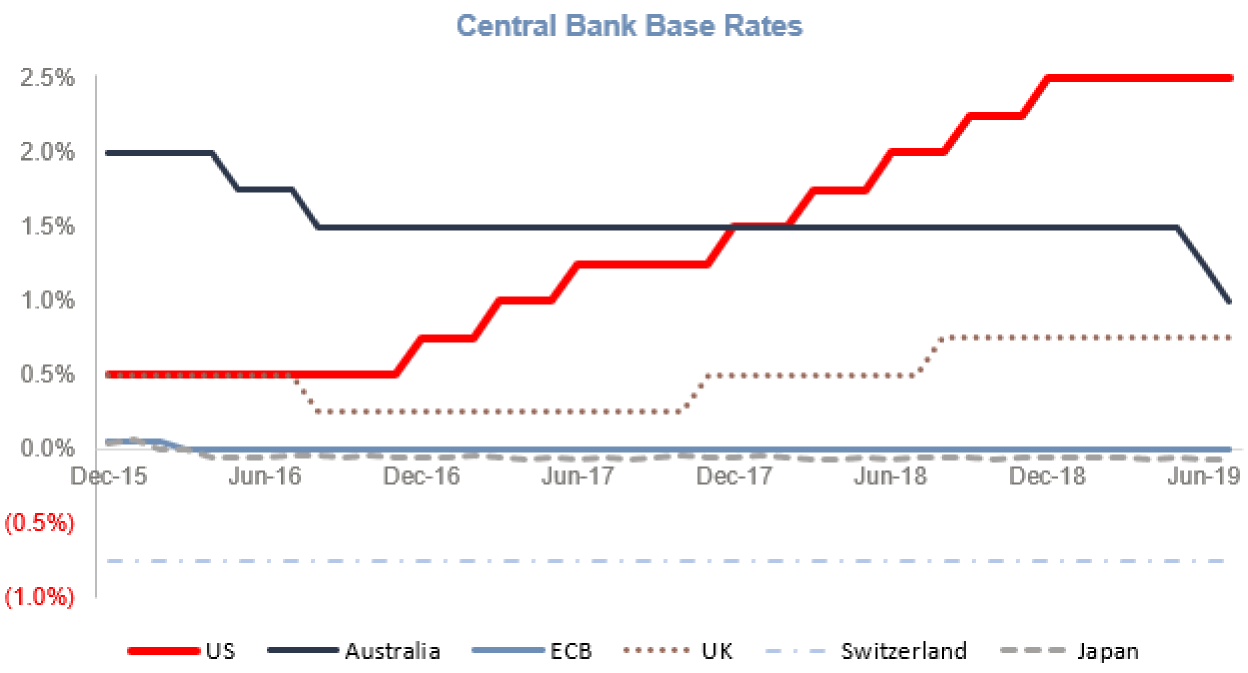
Currency

VG1 is denominated in Australian Dollars (AUD). We actively manage our currency exposure as our analysis of the economic outlook for Australia evolves relative to the US, Europe, the UK and Asia. Our purposeful and active management of the currency has enhanced the VGI Partners Master Fund's total return by 20.7% since inception.

Over the year to June 2019, VG1's strategic currency positioning, which is based on our proprietary fundamental analysis, contributed **+3.3%** to returns as the USD strengthened relative to the AUD.

We continue to believe that the US Dollar remains attractive relative to the Australian Dollar.

The strong US Dollar is ultimately the result of the US outperforming other economies. As a result of US economic outperformance, its interest rates have increased and are now higher than most other developed nations, triggering purchases of the USD due to capital inflows. The below chart demonstrates that the US central bank has increased rates at a much faster pace than other developed economies.



Source: Bloomberg & VGI Partners analysis.

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It has quickly become the consensus view that the US Federal Reserve (Fed) has reached the end of a tightening cycle, and continued trade frictions with China will result in significant rate cuts over the next twelve months. While we do expect the Fed to cut rates, you can see from the above chart that the US Federal Funds rate is still substantially higher than other major central bank rates.

We expect this to remain the case, as the US continues to see a meaningful pickup in inflationary pressure. Most notably, the US is now seeing wage growth acceleration for the first time in over a decade. With the US unemployment rate at 50-year lows of 3.7%, and job growth remaining strong, we expect this wage growth acceleration to continue.

Source: US Bureau of Labor Statistics & VGI Partners analysis.

In our prior letter, dated 29th January 2019, we went against consensus in highlighting our view that the slowdown in Australian housing was likely to drive rate cuts from the Reserve Bank of Australia (RBA). Since this time, the RBA has cut the Cash Rate twice, to just 1.0%.

We now believe that it is highly unlikely that the RBA will reverse direction as we see signs of continued deterioration in the Australian economy. As we have highlighted in the past, Australian households have been on an unsustainable debt binge over recent years, which has flattered the economic statistics. This can be seen in the declining household savings rate.

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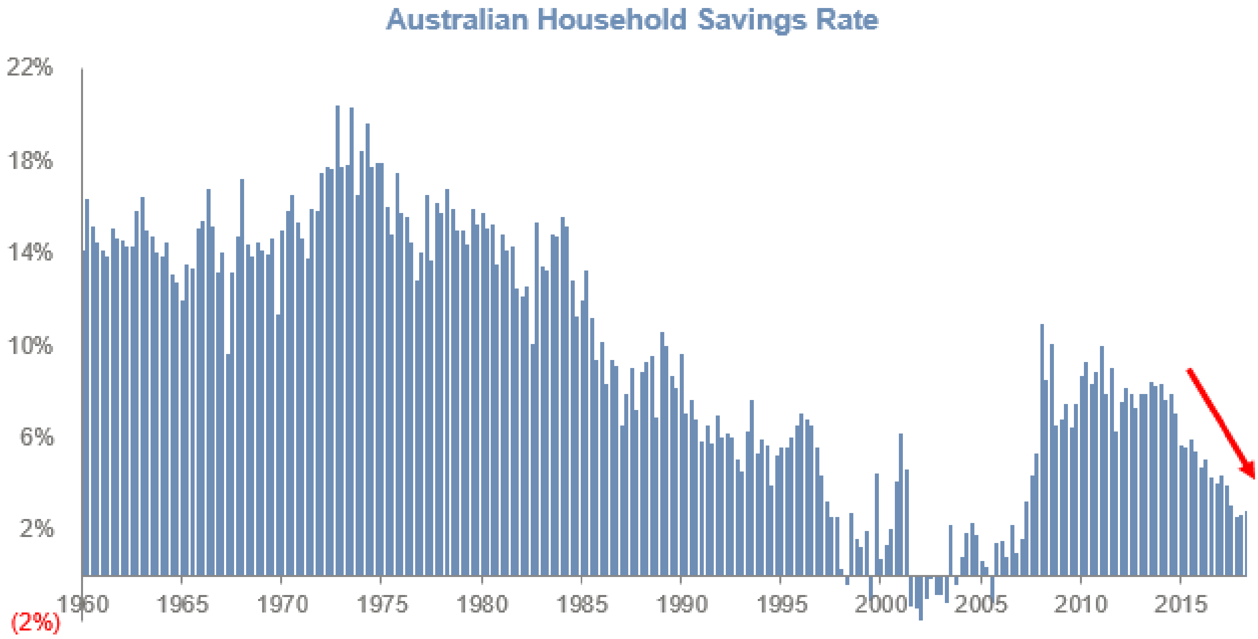
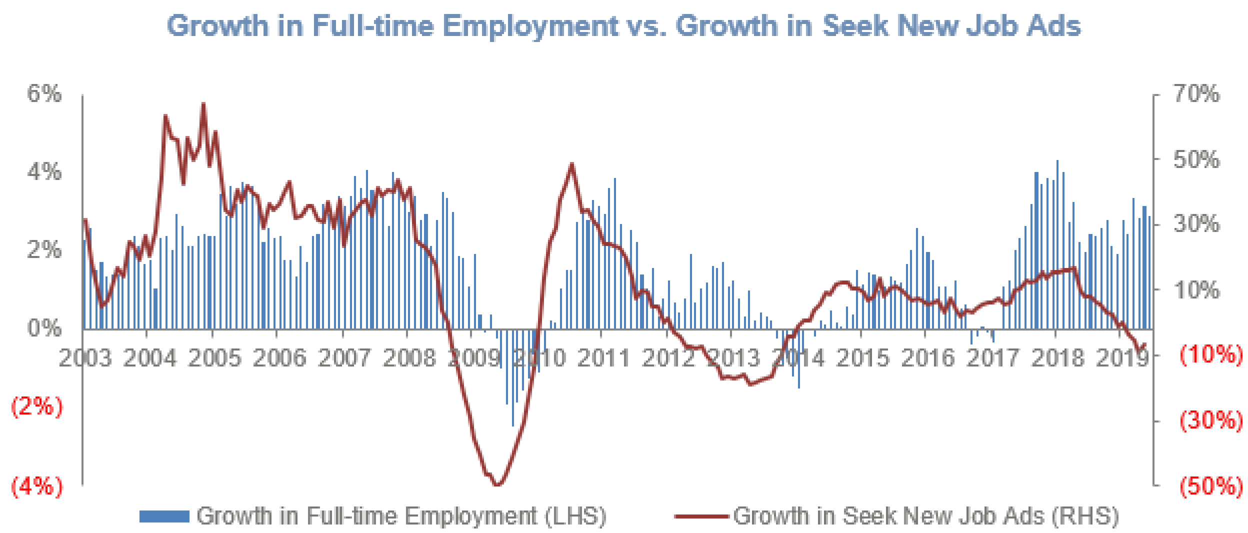


Source: Australian Bureau of Statistics & VGI Partners analysis.

We believe we are now at the start of an unwind of this period of excess. In particular, Sydney home prices have now fallen 15% from peak levels, while Melbourne home prices are down 11% from peak. As a result, we have begun to see the household savings rate stop declining over recent quarters, which bodes poorly for growth in consumer spending.

The RBA has predicated future rate cuts on the pace of Australian job growth. Importantly, the lead indicators we track for Australia are pointing to a slowdown in job growth from here.



Source: Australian Bureau of Statistics, Seek & VGI Partners analysis.

With a long-term view, we also believe Australia's high minimum wage undermines its long-term economic competitiveness. According to the OECD, Australia now has the highest minimum wage in the world.

Australia has a minimum wage of A$19.49 per hour. This is equivalent to US$14 per hour, or almost double the US Federal minimum wage of US$7.25. This simplistic analysis actually understates the minimum wage gap. Under Australia's Award system, it has thousands of minimum wages across various industries, many higher than A$19.49. Australia also has a generous system of superannuation, casual loadings and weekend penalty rates on top of the minimum wage.

The Australian Government has recently put through unusually large increases to the minimum wage (+3.3% from 1 July 2017, +3.5% from 1 July 2018 and +3.0% from 1 July 2019). We believe this is providing a one-off boost to Australian wage growth. Despite this, wage growth remains at historically low levels. This is particularly problematic in light of Australia's huge household debt burden.

Partly as a result of high minimum wages, Australia's total private sector wages remain globally uncompetitive at current exchange rates. In fact, the AUD/USD would need to fall to $0.55 (a fall of 20%) for overall Australian private sector wages to be at parity with the United States.

At some point in the future we will progressively re-hedge VG1's foreign currency exposure. However, this will not happen until our fundamental analysis suggests that the AUD is more fairly valued.

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Company Meetings

Over the past twelve months the VGI Partners' sixteen-person Investment Team conducted over 500 meetings and conference calls with company management teams and industry experts around the world. Our travels took us to the UK, Japan, Singapore, South Korea, Vietnam and across the United States. We met with companies such as Kirin, Becle SAB (which owns Jose Cuervo tequila), Omron, Superdry, Rolls Royce, Citizen Watch and L'Occitane, as well as speaking to a wide variety of industry experts.

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Operational update

As discussed earlier in this letter, two major operational projects were completed over the past six months as we worked towards the listing of VGI Partners Limited (ASX: VGI or the Manager) on the ASX while also undertaking an associated $300 million equity raising in VG1.

In late June we welcomed more than 5,000 new shareholders to VGI Partners on completion of the IPO and, as a result, the vast majority of recipients of this letter are now investors in VGI Partners in addition to their VG1 investment. We are delighted to have delivered on our objective of further strengthening alignment between our investors and VGI Partners itself.

It is testament to the bench strength we now have across VGI Partners that we were able to complete these transactions with only minimal involvement from the senior members of our Investment Team, allowing them to maintain their focus on the portfolio at all times. This is consistent with the intention of the Directors of VGI Partners to measure the Company's success by the long-term returns that we deliver for investors in the VGI Funds in the expectation that shareholder returns will follow. VGI Partners prides itself on fostering a culture of single-minded dedication to this objective.

The VGI Partners team now consists of 26 people across Sydney, New York and Tokyo. We will continue to selectively recruit outstanding people to join the team.

New additions to the VGI Team over the past six months include **Ingrid Groer**, who joined us as Investor Relations Manager for our two listed entities – VG1 and VGI Partners – after an extensive career as a research analyst at Goldman Sachs. Also in Sydney, **David Symons** is now an Investment Director having served on the VGI Partners Advisory Council for the preceding three years. David has twenty years' experience in investment banking, corporate strategy and corporate affairs.

In New York, **Claudia Cole** has joined us as a senior trader while **Nikolay Aleksiev** brings more than ten years as a data scientist to his role as an Analyst – Data & Analytics.

Expansion in Tokyo has also been a feature of the last six months as two new Investment Analysts have joined the team. **Kanta Matsuo** joined us from the research division of Goldman Sachs, while **Bryan Oh** is a recent graduate of Brown University, where he majored in Applied Mathematics and East Asian studies.

Victoria Arthur left the VGI Partners team after two years as Investor Relations Manager for VG1. From a standing start Victoria established a comprehensive investor relations function that is the equal of any listed investment company in Australia. We are grateful for her contribution and wish Victoria every success in the future.

The VGI Partners Team now includes eight CFA Charterholders. In addition, **Claudia Cole** recently sat the exam for Level III of the CFA Program in New York, while **Marco Anselmi** has completed the three CFA exam levels and will be awarded his CFA Charter towards the end of this year. The CFA Charter is one of the most highly regarded qualifications an investment professional can earn, requiring completion of a six-hour exam for each of the three levels (pass rates for each of these exams are typically well below 60%).

Ensuring that we have relationships with the most appropriate suppliers and counterparties is fundamental to VGI Partners' ongoing success. All suppliers and counterparties undergo regular review and new relationships are established when required to support the development of the business and meet client needs. To that end, following a nine-month process, VGI Partners has agreed on commercial terms with Goldman Sachs as an additional Prime Broker and the onboarding process is now underway.

VGI Partners hosted its annual Advisory Council meeting in Washington in May of this year. The VGI Partners' Advisory Council (which was previously known as the Advisory Board) consists of an external and independent group of experienced investment management, finance and industry professionals.

This year we were delighted to welcome as special guests:

- **The Hon Joe Hockey,** Australian Ambassador to the USA
- **Mr John Brennan,** Former Director of the Central Intelligence Agency (2013-2017)
- **Mr Ian Cook,** Executive Chairman, Colgate-Palmolive Co
- **Mr Benjamin Krasna,** Deputy Head of Mission, Embassy of Israel to the US

This meeting provided the Partners with a great opportunity to discuss investment ideas as well as important themes in financial markets and the US political landscape.

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In Closing

At VGI Partners we are entirely focussed on managing our portfolio, which contains our best investment ideas from around the world. We are highly selective about what we include in our portfolio and unemotional about when we should divest an investment.

Our unwavering commitment is to preserve your capital over the long term, regardless of the market environment, by owning high-quality assets which have been purchased with a margin of safety. We cannot eliminate short-term volatility from our returns however we are confident our process and investment philosophy positions our portfolio to produce acceptable returns even when global stock market indices are lacklustre.

We remain optimistic about our existing portfolio and will continue to take advantage of opportunities that present themselves in times of fear and panic. We are very grateful that we have long-term oriented investors who entrust us with their capital.

Since listing in September 2017, VG1 has generated a compound annual return, net of all fees, of **+11.2%** with a monthly average net equity exposure of 41%. We are pleased, but not satisfied!

Once again, we thank you for your investment with VGI Partners.

Yours faithfully,

VGI Partners

"John Bull can stand many things but he cannot stand two per cent."

- Walter Bagehot, the famed 19th-century editor of The Economist, expressed savers' traditional distaste for very low interest rates.

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Forward-looking statements

This document contains certain "forward-looking statements" that are based on management's beliefs, assumptions and expectations and on information currently available to management. Forward-looking statements can generally be identified by the use of forward-looking words such as, “expect”, “anticipate”, “likely”, “intend”, “should”, “could”, “may”, “predict”, “plan”, “propose”, “will”, “believe”, “forecast”, “estimate”, “target” “outlook”, “guidance” and other similar expressions. Indications of, and guidance or outlook on, future earnings or financial performance are also forward-looking statements. You are cautioned not to place undue reliance on forward-looking statements. Any such statements, opinions and estimates in this document speak only as of the date of this document and are based on assumptions and contingencies and are subject to change without notice, as are statements about market and industry trends, projections, guidance and estimates. Forward-looking statements are provided as a general guide only. The forward-looking statements contained in this document are not indications, guarantees or predictions of future performance and involve known and unknown risks and uncertainties and other factors, many of which are beyond the control of VGI Partners, and may involve significant elements of subjective judgement and assumptions as to future events which may or may not be correct. There can be no assurance that actual outcomes will not differ materially from these forward-looking statements. No representation, warranty or assurance (express or implied) is given or made in relation to any forward-looking statement by any person (including VGI Partners or any of its directors, officers, employees, agents or advisers). In particular, no representation, warranty or assurance (express or implied) is given that the occurrence of the events expressed or implied in any forward-looking statements in this document will actually occur. Except as required by law or regulation, VGI Partners disclaims any obligation or undertaking to update forward-looking statements in this document to reflect any changes in expectations in relation to any forward-looking statement or change in events, circumstances or conditions on which any statement is based.