Integrity Transparency Conviction

Clime Smaller Companies Fund

Monthly Investment Report - April 2018

Clime Asset Management Pty Limited
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Investment Objective

The objective of the Fund is to generate sustainable long-term capital growth. The Fund seeks to achieve an annual total return of 8% above the Australian Consumer Price Index (CPI) over rolling five to seven year investment periods after management fees.

Investment Strategy

The Clime Smaller Companies Fund seeks to deliver strong risk-adjusted total returns by investing in a portfolio of high quality smaller Australian companies that are attractively priced.

Fund Profile (Wholesale^)

Investment Manager	Clime Asset Management Pty Limited
Investments	The Fund invests in those companies that are outside of the S&P/ASX200 Index and above $50m market capitalisation at the time of establishing a position.
Inception Date	24 April 2017
Income Distributions	Annual. Unless otherwise requested, distributions are automatically reinvested.
Management Fee	1.03% p.a.^^
Contribution Fee	Nil
Minimum initial investment	$100,000
Minimum additional investment	$10,000
Minimum balance	$100,000
Expenses	0.21% p.a.
Withdrawal Fee	Nil
Performance Fee	Performance Fee of 20% of Fund's total return above investment objective of CPI^^^ + 8% pa inc. GST.
Investment Horizon	Suggested minimum 5 years

^As defined by the Corporations Act
^^The Clime Smaller Companies Fund is currently in the incubation phase, during which time the manager will be charging reduced management fees. This will be reviewed on a (calendar) quarterly basis.
^^^Trimmed mean Consumer Price Index as measured by the Reserve Bank of Australia

Portfolio Total Return (30/04/18)

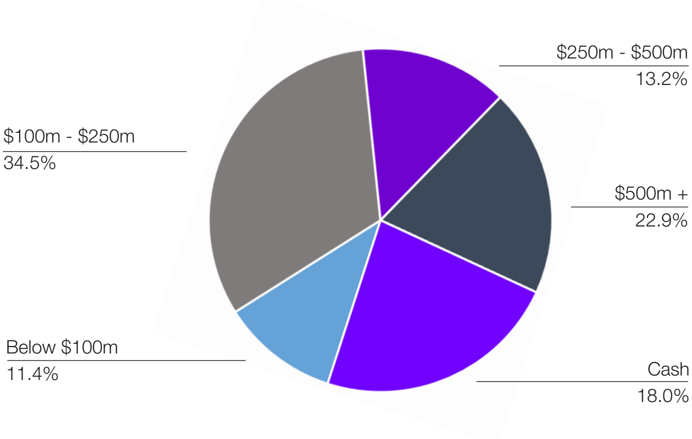
	Portfolio Return	Fund Objective^
1 month	0.35%	0.78%
3 months	1.28%	2.33%
6 months	7.97%	4.80%
1 year	21.97%	9.86%
Inception*	21.66%	9.87%

* Inception: Wholesale Units: 24 April 2017. Performance figures for more than 1 year are annualised, calculated after all applicable fees and taxes. Returns have been calculated based on starting and ending unit prices after taking into account all ongoing fees, and assuming reinvestment of distributions. ^ CPI + 8% p.a. including GST.

Distributions

Period Ending	**Wholesale Units (cents per unit)**
30 June 2017	0.1564

Asset Allocation by Market Capitalisation



Prominent Fund Holdings *(alphabetical order)*

bravura solutions	Bravura Solutions Limited (ASX: BVS)
Elanor Investors Group	Elanor Investors Group (ASX: ENN)
HANSEN TECHNOLOGIES	Hansen Technologies Limited (ASX: HSN)
JUMBO	Jumbo Interactive Limited (ASX: JIN)
NAVIGATOR GLOBAL INVESTMENTS	Navigator Global Investments Limited (ASX: NGI)

Summary

The Clime Smaller Companies Fund (CSCF) delivered a modest return of 0.4% (net of all fees) for the month. The CSCF has delivered a return of 18.8% (net of all fees) for the financial year to date (FYTD).

During the month of April, the CSCF enjoyed its first birthday. While we are encouraged by the start, our objective is to report solid results to co-investors over a much longer-term time frame. With that noted, small milestones often give one the opportunity to pause, reflect and refocus on these long-term objectives. We therefore marked the occasion by penning a 'Letter to Investors'. In this note, we convey our thoughts to co-investors on the journey thus far, review the portfolio's positioning and consider the outlook in the context of what we see as a more volatile investing landscape.

One of the first positions initiated in the Fund was that of Collins Foods (ASX: CKF), a business largely focused on the operation, management and administration of KFC restaurants across Australia, Germany and the Netherlands.

With CKF having just completed the end of its financial year on the 29th of April 2018, now is perhaps a good time to revisit the investment case for the business. Though only listed on the ASX since 2011, Collins has been around since the 1960s, having obtained its first KFC franchise in 1968. In the decades since, CKF has steadily grown its footprint and is now one of the more prominent KFC focused franchise operators in the Australian market (at around 30% KFC network share).

In recent years, CKF has continued to build out its domestic presence via a greenfield store roll-out program and selective acquisitions. Inclusive of recent acquisitions, CKF's KFC Australian store network has grown substantially to 225. Over the next three to five years, we expect this network to grow organically by around eight stores per annum.

Management has also taken decisive action in recent years to invest in what will likely become the next key driver of growth for the company: Western Europe. As at the half year, CKF had a total of 31 KFC restaurants, split between 15 in Germany and 16 in the Netherlands.

CKF are also guiding to a considerable greenfield store roll-out in each country, having suggested the business is 'on target to open 3 to 4 in Germany and 3 to 4 in Netherlands during 2018 calendar year.' While coming off a smaller base, this implies a substantial long-term growth opportunity in markets deemed underpenetrated by both YUM! Brands (NYSE: YUM) and CKF management.

Beyond KFC Australia and Europe, a new opportunity on the horizon is that of Taco Bell, another leading Quick Service Restaurant (QSR) brand from the stable of YUM. Though management are doing their best to temper expectations, we understand CKF's first Taco Bell store continues to trade well above initial forecasts.

CKF has two further stores scheduled to open this calendar year. While at an early stage, if subsequent stores prove to be as successful as CKF's initial Annerley restaurant, we see significant scope for a further meaningful store roll-out over the next five to seven years.

We have long been attracted to the consistent cash flow profile of the CKF business, which has proved resilient since listing on the ASX. In turn, this has allowed the business to sensibly utilise gearing to generate sound returns on shareholder equity.

Given recent acquisitions have been partially debt funded, we expect that the net leverage ratio (measured as net debt/EBITDA) will approximate 2.1x at (financial) year end. We see this as towards the top end of management's preferred gearing range. As a result, we are looking for management to sensibly strike the right balance between the payment of dividends and reinvesting retained earnings to drive growth, while also steadily de-gearing the business in the coming periods.

While we expect CKF's June full year results announcement to reflect steady aggregate growth, we are more excited about the long-term prospects for CKF's multiyear store roll-out opportunity. When coupled with moderate growth in same store sales and likely incremental scale benefits, we believe CKF can generate double-digit earnings growth over the medium-term.

Although much remains to be executed, given a solid track record, a strong existing foundation and an experienced management team we believe CKF can potentially become a much larger business in the years to come.

In the days either side of month end, portfolio constituent Citadel Group (ASX: CGL) delivered several positive updates that further strengthen the investment case. For the uninitiated, CGL is focused on the delivery of managed technology solutions for a high-quality customer base operating in the Government, Defence, Health and Education sectors.

CGL was established in 2007 and listed on the ASX in 2014 with a board and senior management team whose experience and quality would rival most ASX100 companies. This includes former Macquarie Bank Chairman Kevin McCann, retired Lieutenant General Peter Leahy AC and CGL co-founders Mark McConnell and Miles Jakeman, both of whom have defence and intelligence backgrounds (respectively).

Like several other CSCF investments, we are attracted to the solid degree of revenue visibility within the business. The majority of CGL's revenue is generated from long-term managed services and Software-as-a-Service (SaaS) solutions, with contracts typically spanning about five years.

Specific to the recent update, CGL effectively reaffirmed full year consensus earnings estimates, implying the business expects to deliver a strong second half result. CGL concurrently announced another 10-year information management contract with a large Government organization as well as a small bolt-on acquisition for its Health business unit.

Our valuation range of $6.70 to $7.00 per share reflects the generally positive outlook, with profit and profitability forecast to continue improving over the medium term. Due to the nature of its business and business relationships, we believe CGL's strategic growth plans can be achieved with little dependence on the broader economic environment.