Integrity Transparency Conviction

Clime Smaller Companies Fund

Monthly Investment Report - May 2017

Clime Asset Management Pty Limited
Level 7, 1 Market Street Sydney NSW 2000

PO Box Q1286, QVB
Sydney NSW 1230

Phone 1300 788 568
www.clime.com.au

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 and is expected to be in place until the fund size reaches A$10 million.

^^^Trimmed mean Consumer Price Index as measured by the Reserve Bank of Australia

Portfolio Performance (31/05/17)

	Portfolio Return
1 month	0.94%
3 months	-
6 months	-
1 year	-
Inception*	1.00%

* Inception: Wholesale Units: 24 April 2017. Performance figures for more than 1 year are annualised, calculated after all applicable fees and taxes. Performance figures compare unit price to unit price for the given period. The returns do not include the benefit of franking credits.

Summary

Dear Fellow Unitholders

It is with great pride that we write the first monthly report for the Clime Smaller Companies Fund (CSCF or the Fund). With the Fund being officially launched on 24 April 2017, May represented the first full month of operation for the Fund. As you might expect, we have taken a measured approach to investing capital thus far. We closed the month with approximately 84% held in cash.

Before delving into market and portfolio specific commentary, we thought it would be worthwhile reiterating the philosophical underpinnings of the CSCF. At its core, this Fund is focused on finding great companies early in their development cycle. In recent years, participants across the global investment landscape have been challenged by an environment where reasonably priced, genuine growth has been very hard to come by. The era of extremely low interest rates has corralled many Australian investors into higher yielding domestic large cap equities. Despite their modest growth profiles, many such companies currently command healthy valuation premiums.

Such an environment lends itself to the launch of a fund such as the CSCF, which will seek to take advantage of what we believe to be neglected, under-appreciated growth opportunities typically more prevalent outside the ASX's major indices. More specifically, the CSCF seeks to deliver strong risk-adjusted total returns by investing in a portfolio of high quality, attractively priced smaller Australian companies that reside outside of the S&P/ASX 200 investment universe.

It is worthwhile noting that we are not seeking to 'recreate the wheel' when considering the Fund's investment process. While a new fund, the CSCF will be managed in line with Clime's existing investment framework, though exclusively applied to a subset of companies outside the ASX200 index. Our focus therefore remains on characteristics such as competitive advantage, balance sheet strength, cash generation, management quality and favourable future prospects.

Furthermore, the CSCF seeks to take advantage of what we believe to be a structurally inefficient market segment. Within the Australian investment universe, small and micro cap equities typically have limited research coverage, reflecting the lower commission potential on offer for traditional brokerage business models.

Concurrently, lower levels of liquidity prevent large institutions from meaningful participation in this market segment. The traditional institutional asset management approach continues to focus on benchmark-relative investing and maximising profitability via increasing funds under management rather than preserving high returns for clients. In aggregate, we believe this creates the opportunity for value-based, focused smaller company investors. While we may hold up to a maximum of 40 securities, we believe that over time the fund will typically hold between 15 and 25 securities. Specific weightings will broadly reflect our perception of the quality and value on offer, as well as prudent risk management. We anticipate assigning larger portfolio weightings to select opportunities that offer considerable downside protection concurrent with longer term growth opportunity.

A clear focus on capital preservation has long been one of the cornerstones of Clime's investment philosophy. At its core, Clime's investment process seeks to mitigate risk by acquiring a part share in a diverse range of high quality businesses at meaningful discounts to our calculated intrinsic future value.

The Fund is not required to be fully invested. At times, the levels of cash or cash equivalents may be high (up to 100%) where attractive investment opportunities are not apparent and/or elevated market uncertainty presents an increased risk of near-term capital loss. The Fund's cash holding seeks to preserve capital and provide the ability to pursue selective investment opportunities as they become apparent.

In terms of market performance, following a modestly positive start to the calendar year, the month of May presented investors with markedly tougher market conditions. All domestic indices fell by a reasonable margin during the month, with the Small Ordinaries accumulation producing a return of -2.1%. The absolute-return focused, cash heavy CSCF fared reasonably well, generating a return of 0.94% for the month.

While many factors exert pressure on equity pricing at any given time, we believe one of the more pervasive factors currently impacting Australian investors is what seems to be faltering discretionary spending. We see a growing disconnect between wages, the growth of which (in real terms) remains tepid at best, and the real cost of living. Many household bills related to utilities, healthcare, education and childcare continue to increase at rates well in excess of wage growth. Concurrently, we continue to observe a household sector whose debt as a percentage of household disposable income, at just under 190 percent, has never been higher (Source: RBA).

Dissecting the Australian population into three broad categories further highlights why we believe pressure continues to build on discretionary spending. Those without a mortgage are arguably saving a greater percentage of after tax earnings to fund a deposit in a housing market that looks excessively priced. Those that have mortgage debt, typically have a lot of it and are seeking to repay this at rates above the minimum. Those either in or approaching retirement have seen the return (interest) generated on lower risk assets (such as cash) diminish to very low levels and as a result, this group may be more inclined to reduce or defer spending.

The end result is that we see consumers of varying demographics under differing forms of pressure; consumers that on average have pared back expenditure, reflecting increased levels of caution and reduced confidence. The subsequent ripple effect appears to be permeating the Australian economy and is more recently being reflected in the equity pricing of consumer related ASX listed businesses. It is by no means all 'doom and gloom'; we believe there are investment opportunities. We see the market environment starting to reflect some of these challenges, and we are beginning to see some pockets of select high quality opportunity. With that said, we remind investors that the strategy and process employed by the Manager very much reflects a long term view.

The Fund's recommended investment time frame is 5 to 7 years. We have little doubt that at some future point we will endure challenging times. These challenges also bring opportunity and it will be the enduring focus on the fundamental process, the diligence to complete the research and the patience to hold the spotlight on a long-term horizon that will build value over time.

We look forward to the journey and again thank you for entrusting your capital with us.