Integrity Transparency Conviction

Clime Smaller Companies Fund

Quarterly Investment Report - June 2018

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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

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

Portfolio Total Return (30/06/18)

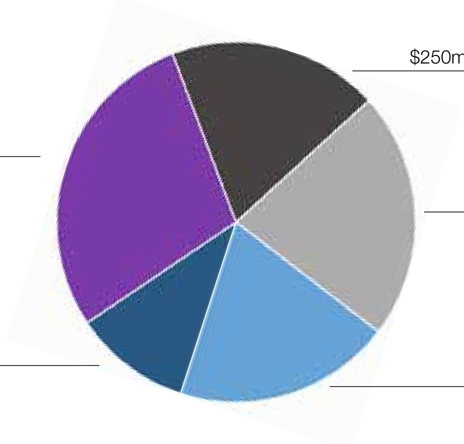
	Portfolio Return	Fund Objective^
1 month	0.62%	0.78%
3 months	3.14%	2.38%
6 months	6.57%	4.80%
1 year	22.05%	9.90%
Inception*	21.12%	9.87%

* 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 2018	4.3495
30 June 2017 (Inception 24/04/17)	0.1372

Asset Allocation by Market Capitalisation



Prominent Fund Holdings *(alphabetical order)*

Axsesstoday Limited (ASX: AXL)

Bravura Solutions Limited (ASX: BVS)

Elanor Investors Group (ASX: ENN)

Jumbo Interactive Limited (ASX: JIN)

Navigator Global Investments Limited (ASX:NGI)

Summary

The Clime Smaller Companies Fund (CSCF) delivered a return of 0.6% (net of all fees) for the month and a return of 22.1% (net of all fees) for the 2018 financial year.

While geopolitical trade tensions remain concerning, supportive economic data releases and constructive underlying company earnings across major regions, coupled with generally positive investor sentiment, have seen broader equity markets continue their steady upwards trajectory.

The leadership position of the US Federal Reserve and its Chair, Jerome Powell, in maintaining their resolve to gradually increase interest rates sets a tone for what we believe will ultimately provide greater stability in global financial markets and hence support more efficient (medium-term) capital allocation decisions. The European Central Bank provided its clearest signs to date of developing a program to ease and ultimately end its bond-buying stimulus program.

This supports our view of longer-term bond yields gradually moving higher (bond prices lower), notwithstanding some oscillation – as was the case over the June quarter – driven by increased volatility and investor uncertainty.

The unconventional policy actions of the Trump Administration continue to be a cause for investor concern. While history will ultimately determine the effectiveness of these policy actions, Trump's 'doubling down' on stimulatory tax cuts in the latter part of 2017 at the time of US Fed Reserve rate rises, and continued rhetoric on tariffs and trade restrictions in 2018 to date have most certainly been a key driver of global investment markets and amplified global market uncertainty and hence volatility.

Domestically, investors seem to be steadily moving beyond the fallout from the Financial Services Royal Commission's 'banking behavior in the spotlight', with major banks recovering strongly during the month of June. Proposed political policy, most notably from the Federal Opposition, continue to provide a source of considerable investor concern. Beyond the cessation of franking credit refunds, further concerns resulted from an initial pledge to repeal small business tax cuts from the Federal Labor Party.

Australian equities ended financial year 2018 with a flurry, driven by global, regional and local buying support, particularly during the latter part of the month of June.

Smaller ASX-listed industrial companies enjoyed a solid level of support during the month of June, building further on the positive returns generated in the 2018 financial year to date. One unfortunate exception was Hansen Technologies (ASX:HSN), whose FY2018 trading update left many reassessing their forecast earnings assumptions.

HSN is a global provider of mission critical billing software solutions. One of its great attractions is its tendency to become embedded in the operations of its customer base, who primarily operate in the energy, water, telecommunications and Pay TV sectors. As a result, customer churn is extremely low while the proportion of recurring revenue is high.

HSN's trading update contained two key components:

1. *For FY18, expectations are for operating revenue of approximately $230 million and earnings before interest, tax, depreciation and amortisation (EBITDA1) of approximately $58 million, giving an EBITDA margin of around 25%.*
2. *For FY19, notwithstanding that growth in underlying recurring revenue is anticipated, at this stage total revenue is expected to be slightly below FY18 because of:*
   a. *termination of the call centre contract within the Solutions business referred to above – which will result in the loss of approximately $1.8 million of revenue in FY19 compared with FY18; and*
   b. *returning to a normalised level of project revenue following the elevated level achieved in FY18 (particularly 1H18).*

The second component of the announcement was perhaps the more disappointing element of the update, which has caused a meaningful rebasing of growth expectations. However, while noting our disappointment, our long-term investment thesis remains intact. The reality is that although HSN has near 100% customer retention, the business grows largely via acquisitions. HSN has an excellent track record at acquiring sensibly and substantially lifting margins of acquired businesses.

To date, our strategy for HSN has been to accumulate at prices that imply low/no assumptions around future acquisitive growth. Given the substantial retracement in price, we now believe this to be the case. This assertion is strengthened by our belief that HSN can and will continue to improve the margins of the recently acquired Enoro business.

Acknowledging all of the above and after factoring in the new information received, we reduced our FY2019 valuation, however, we retain a positive long-term view. As a result, we made the decision to incrementally add to our portfolio position.

A significant bright spot for the portfolio during FY2018 was that of Bravura Solutions (ASX: BVS). Though it has been years in the making, BVS is today a leading global provider of enterprise software and Software-as-a-service (SaaS) to the wealth management, funds administration and life insurance industries.

The core software platform provided by BVS, Sonata, continues to replace ageing legacy systems while gaining market share in its key geographies of Australia, New Zealand, South Africa and the UK. BVS won two large new contracts during the June quarter; Commonwealth Superannuation Corporation (Australia) and Legal & General Investment Management (UK), both of which are on long-term contracts.

The consistent growth in the customer base of BVS, when coupled with increased engagement with its existing clientele, continues to drive expectations for further revenue growth and margin expansion in the coming years. BVS remains on track to deliver approximately 18% earnings per share growth in FY2018, a figure we expect to be broadly replicated over the medium-term. As such, BVS still presents as a long-term compounding opportunity.

Also noteworthy during the month of June was the full year result of Collins Foods (ASX: CKF). The core business of CKF relates to the operation, management and administration of KFC restaurants across Australia, Germany and the Netherlands.

While not a spectacular result, the business continues to execute credibly on its growth plan, having delivered growth of 13% in underlying profit to $38.9m. Cash generation was again a highlight, with operating cash flow up 23% to $74.5m.

As articulated previously, our investment thesis primarily relates to the opportunity for the business to reinvest its substantial cash flow into organically growing the store network. To that end, management have indicated that they expect to roll out approximately 14 to 16 greenfield sites across all core geographies annually. This equates to organic footprint growth of about 6% per annum.

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. While much remains to be executed, given a sound track record, experienced management and a strong existing foundation, we believe CKF can become a much larger business in the years to come. Our valuation remains a comfortable margin above the share price. So in our view, CKF still offers investors sound prospective returns at current prices.

After delivering a solid first full financial year and associated distribution, we enter the new financial year well-positioned to steadily build on the platform laid thus far. While the financial year has ticked over, our focus remains the same. We continue to seek out, focus on and accumulate ownership stakes in a growing range of high quality companies trading at discounts to intrinsic value.