Ophir High Conviction Fund

ASX: OPH

www.ophiram.com

INVESTMENT UPDATE AND NAV REPORT – FEB 2019

The Ophir High Conviction Fund seeks to provide investors with a concentrated exposure to a high quality portfolio of listed companies listed outside the S&P/ASX 50. Employing an extensive investment process that combines a rigorous company visitation schedule and fundamental bottom-up analysis, the Fund aims to identify businesses operating within structural growth sectors with the ability to meaningfully grow and compound earnings over time. Typically, the majority of businesses within the portfolio will already have well-established business models with large or growing end markets and a clearly identifiable pipeline of future growth opportunities. As a concentrated portfolio, the Fund seeks to identify the very best of these opportunities in order to ensure each portfolio position delivers a meaningful impact on overall portfolio returns.

ASX Code	Net Per Annum Return Since Inception (to 28 Feb 19)	Net Return Since Inception (to 28 Feb 19)	Fund Size (at 28 Feb 19)
ASX:OPH	**21.1%**	**98.0%**	**$495.8m**

FEBRUARY 2019 PORTFOLIO SNAPSHOT

NET ASSET VALUE (NAV) PER UNIT

As at 28 February 2019	Amount
NAV	$2.47
Unit Price (ASX:OPH)	$2.56

To access daily NAV prices for the Ophir High Conviction Fund (ASX:OPH), historical ASX announcements and performance history, please visit www.ophiram.com

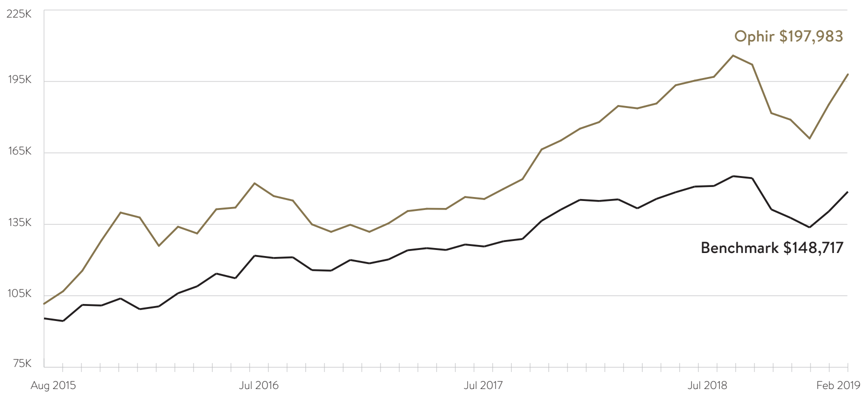

*Chart represents the value of $100,000 invested since inception after all fees and before tax and assuming distributions are reinvested in the Fund. Performance of the Fund is calculated using Net Asset Value (NAV), not the market price. Please note past performance is not a reliable indicator of future performance.

INVESTMENT PERFORMANCE

	1 Month	FYTD	1 Year	2 Years p.a.	3 Years p.a.	Since inception p.a.
Ophir High Conviction Fund	**7.2%**	**2.9%**	**9.7%**	**23.7%**	**18.7%**	**26.1%**
Benchmark	5.9%	-1.4%	2.2%	9.2%	13.9%	11.7%
Value Add (Gross)	1.3%	4.3%	7.5%	14.5%	4.8%	14.3%
Fund Return (Net)	6.9%	1.4%	7.2%	20.9%	16.3%	21.1%

Performance figures are calculated using the Net Asset Value (NAV) of the Fund as at 28 Feb 2019, not the market price. Benchmark is the ASX Mid-Small Accumulation Index. Inception date of the Fund is 4 August 2015. Past performance is not a reliable indicator of future performance.

TOP 5 PORTFOLIO HOLDINGS (ALPHAETICAL)

Company	Industry	ASX Code
The A2 Milk Company	Consumer Staples	A2M
Afterpay Touch Group	Financials	APT
Cleanaway Waste Management	Industrials	CWY
Reliance Worldwide	Industrials	RWC
Seven Group Holdings	Industrials	SVW
Average Portfolio Market Cap		**$4.45bn**

KEY INFORMATION

Responsible Entity	The Trust Company (RE Services) Limited
Manager	Ophir Asset Management
Portfolio Managers	Andrew Mitchell & Steven Ng
Fund Inception	4 August 2015
Fund Size	$495.8m
Number of Stocks	15-30
Cash Distributions	Annually

ALLOCATION OF INVESTMENTS

PORTFOLIO SECTOR EXPOSURES (as at 28 Feb 2019)

Sector	28 Feb 19
Materials	11.53%
Financials	0%
Health Care	4.67%
Communication Services	2.18%
Consumer Staples	10.46%
Information Technology	14.84%
Industrials	18.04%
Consumer Discretionary	26.25%
Utilities	0%
Real Estate	0%
Energy	0%
[Cash]	12.04%
	100%

MARKET COMMENTARY

Equity markets continued their strong positive momentum this month, with risk assets globally benefiting from further supportive central bank commentary and the prospect of additional Chinese stimulus measures. US equities, particularly, continued their incredible run from the depths of their December 2018 lows to now posting the best two-month beginning to a calendar year since 1987. The euphoria embracing the region remains relatively market cap agnostic, with both the mega-cap Dow Jones Industrial index and the US small cap Russell 2000 index both posting eight consecutive weeks of positive gains – an outcome not achieved by each index since 1964 and 1984[1] respectively.

A cooling in US-China trade tensions combined with increased expectations for further domestic stimulatory measures has ignited an equally impressive turnaround from Chinese equity markets, the CSI 300 Index (tracking the top 300 companies listed on the Shanghai and Shenzen stock exchanges) rising +14.6% for the month. Indeed, the significant price gyrations experienced across the majority of global equity markets through the final quarter of 2018 now seem a distant memory, with the CBOE Volatility Index having now recorded nine straight weeks of declines – its longest continuous weekly regression on record.

On local shores, a half-yearly ASX reporting period that contained multiple anecdotes of increasingly tepid economic conditions did little to dampen the positive broader momentum toward equities. Helped by a significant post-Royal Commission relief rally across the index-heavy big banks and financials, the S&P/ASX 200 increased +6.0% for the month, while the S&P/ASX Small Ordinaries Index rallied +6.8%.

Strong absolute performances across domestic equities during the crucial company reporting periods of February and August generally tend to be a bullish indicator for near term market direction. One might normally assume that rising share prices (at the same time as 2,000+ companies deliver their periodic half-yearly updates) would indicate a market delighted with broadly better earnings results and improving future outlooks. However February 2019 reporting period has been somewhat of an anomaly in this regard, with the reporting period proving to be somewhat disappointing in aggregate versus consensus, with the bulk of index returns being driven by macro factors.

Indeed, a large bulk of the outsized returns delivered this month came from companies with a high proportion of their register held short that evidently delivered results that were simply 'less worse' than feared. As an indicator of the tough conditions currently facing the majority of domestic-facing businesses in Australia, only 42% of the companies represented in the S&P/ASX 200 delivered any positive earnings growth at all for the first half of FY2019 – the weakest earnings performance by the index since the Global Financial Crisis.

That being said, the challenging conditions facing a wide proportion of Australian businesses at present have been a 'known known' for some time and expectations coming into the reporting period across domestic-facing companies were already suitably low. Earnings estimates for the bulk of Australian housing, building and consumer-facing businesses, for example, had experienced fairly consistent negative revisions coming into the February results period – in effect ensuring the earnings bar had been set reasonably low.

As a result, overall earnings per share (EPS) 'beats' for the February reporting period were roughly in-line with historical averages, although consensus earnings expectations for the second half of the financial year have again been revised materially lower. Sluggish consumer demand (particularly through the final quarter of calendar year 2018), ongoing political and regulatory uncertainty and pockets of rising input cost pressures collectively created a raft of revenue headwinds for businesses facing the domestic economy. While the resources sector – and the mining services and contracting business that service the industry – have enjoyed the benefit of strong commodity prices through the period, both the ASX 200 Industrials and ASX 200 Financials experienced their largest consensus downgrades to full-year growth forecasts since 2009.

Unsurprisingly, the key takeaway after meeting with over 60 companies directly and a further 38 in group settings has been the continuing tough conditions facing businesses reliant on the underlying strength of the Australian economy and/or consumer. While expectations across the building materials, property development and housing-exposed retailers were already low, the pervasive impact from falling East Coast home prices (and the negative flow-on effects to consumer spending) again surprised to the downside. Consumer spending still represents c.60% of total Australian GDP per annum and the varied companies and sectors that have begun to register top line impacts from the consumer/housing slowdown have begun to broaden.

Gaming and entertainment group Crown Resorts (CWN), for example, commented its domestic premium gaming rooms in Sydney and Melbourne experienced softness through the December quarter, while pubs and bottle-shop operator Redcape Hotel Group (RDC) cited an increasing 'variability' in trade across a number of their venues over the September-December period. Automotive parts distributor and retailer Bapcor Limited (BAP) experienced softer performance from their retail and servicing divisions (consumers seemingly willing to defer the scheduled servicing of their cars through the quarter to conserve cash flow), while diagnostic imaging provider Capitol Health (CAJ) blamed a weaker first half result due to a lower number of patients attending GPs through the first half.

Retailers, unsurprisingly, continue to face difficult market conditions albeit a large amount of the negativity had arguably been baked into valuations prior to February. As a result, the sector saw a number of fairly stellar moves upwards from a handful of businesses that delivered on prior earnings guidance amidst a consensus backdrop that had begun to assume peak pessimism. Considerably low expectations and a high level of short interest often proves a lethal catalyst for a share price re-rating, with the retail sector enjoying a number of significant turnarounds from the delivery of earnings 'meets' (not even beats!). Most notable included online travel provider Webjet (WEB, +30.6%), fast fashion retailer Lovisa (LOV, +39%), appliance manufacturer Breville Group (BRG, +45%) and natural beauty products wholesaler BWX Limited (BWX, +54%).

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1 The Russell 2000 was created in 1984 – until 2019, the index has not experienced eight consecutive weeks of positive gains.

Interestingly, despite the continued negativity toward the sector, overall like-for-like sales growth (a measure used to determine the level of sales generated across a retailer's footprint, not including new or divested stores) were not diabolical, while trading updates provided for the first four-to-six weeks of the year appeared cautiously optimistic. In-store foot traffic continues to remain depressed across the majority of domestic retailers, however this has been offset by the continued and persistent growth in online transactions. While the impacts from a sluggish housing market will continue to weigh on consumer confidence near term, the possibility of household incomes receiving some respite near term from pre-election policy boosts may provide the sector with some additional support in coming months.

Outside of relief rallies experienced across some of the more beaten-up cyclical names, it has again been the cohort of Australian businesses with international growth options that delivered the lion's share of earnings growth this period. While the domestic economy continues to face a myriad of growth hurdles near term, Australian businesses with established channels into higher growth offshore markets (particularly the US and Asia) have been amply rewarded for their investment in overseas expansion. An Australian dollar now plumbing multi-month lows (sitting at c. US71c at the time of writing) provides an additional near-term attraction given the currency translation benefit of the AUD/USD retreating a further -4.8% over the first half of the financial year.

Notable performances from more offshore-facing businesses within the Ophir High Conviction Fund included the impressive entry into the United States from modern day lay-by provider Afterpay Touch (APT), the business having now welcomed over 1 million US customers onto the platform (across 2,800+ retailers) just 10 months after launching in the country. Fast fashion jewellery retailer Lovisa (LOV) pleasingly recorded strong sales growth across a number of new territories in Europe and the USA (the business adding 12 additional stores in the UK, 5 stores in France, 3 stores in Spain and 7 in the US), while infection prevention medical device company Nanosonics (NAN) announced a further +9% increase in the global installed base of their infection prevention device 'trophon', including Europe, Asia, Australia and North America.

PORTFOLIO COMMENTARY

The Net Asset Value (NAV) of the Ophir High Conviction Fund increased by 6.9% over the month of February (net of fees and before tax), outperforming its benchmark by 0.9%. Since inception in August 2015, the Fund has returned +21.1% per annum (net of fees and before tax), outperforming its benchmark by 9.3% per annum.

For February, the top contributors to fund performance were electrical consumer products retailer Breville Group (BRG), waste management solutions provider Cleanaway Waste Management (CWY) and mining services and construction conglomerate Seven Group Holdings (SVW)

Key detractors to fund performance versus index this month were salary packaging provider Mcmillan Shakespeare (MMS), data centre operator NextDC (NXT) and plumbing parts supplier Reliance Worldwide (RWC).

We have been happy with the performance of the Ophir High Conviction Fund throughout the reporting period. The results season provides one of the more transparent tests of an investment team's investment process and we take great pride when delivering reasonable returns through the period (and in minimising significant exposure to earnings downgrades). In this regard we have delivered well, with only two earnings/consensus downgrades experienced over the 24 stocks held within the portfolio – a pleasing result.

Additionally, we have been equally pleased that a good number of larger weightings in the Fund (i.e. those business that represent larger positions of the portfolio and ones in which we hold our highest level of conviction) benefitted from earnings upgrades through the month. The portfolio was exposed to earnings upgrades/beats across 6 of the portfolio's holdings that reported earnings this month. Interestingly, despite significant increases in share prices across a number of holdings, the level of conviction in the portfolio continues to remain high: after meeting with 100% of the companies held within the portfolio (that issued earnings updates this month), we continue to retain the same 24 positions we entered February with, while only adding one additional name.

While the outlook for the Australian economy near-term remains challenging, we continue to feel the broader small and mid-cap equities space continues to provide attractive investment opportunities (particularly for those businesses displaying an ability to grow either offshore or independent of the domestic cycle). While conviction in the current portfolio holdings remains high, we remain cognisant that we are operating within a market that is decidedly 'late cycle' and continue to expect further periods of volatility and macro uncertainty from here.

As a result, the portfolio continues to retain a strong bias towards businesses we view as 'higher quality' (sustainable earnings, strong balance sheet, high returns on invested capital and pricing power), and also favours businesses further up the market cap curve.

STOCK NEWS

While businesses facing the US, New Zealand and pockets of Europe have benefitted from broadly stronger economic conditions, it is worth noting some tempering of enthusiasm from companies exporting products and services into China. Economic data through the region has been soft in recent months, while anecdotally a number of China-facing management teams have highlighted increasing levels of domestic competition. Vitamins distributor Blackmores (BKL, not held), blood products manufacturer CSL Limited (CSL, not held) and industrial gloves retailer Ansell (ANN, not held) all mentioned either heightened competition in the region or a noticeable slowing in end user demand.

Seemingly unaffected at this point has been portfolio holding The A2 Milk Company (A2M), the specialist dairy and infant milk formula producer announcing +41% growth in revenues for the first half of the 2019 calendar year and a +58% increase in EBITDA. While now commanding a market capitalisation in excess of $10 billion, it is extraordinary to think that the business only six years ago was a NZ-based fresh milk producer generating $48.6m in revenues for a $210m market capitalisation.

Through exceptional growth in demand for its infant milk formula products into China and a growing fresh milk presence in the United States and the UK, the business is now on track to deliver north of $1.25 billion in revenues for the 2019 financial year – indeed the business now holds more cash on its balance sheet than its entire market capitalisation in 2012.

While China will remain the key growth driver for earnings near term, we are growing increasingly excited with the momentum growing behind the brand in the United States, with fresh milk sales into the region doubling this half over the previous period. With further distribution agreements recently signed with national US supermarket chain Krogers and additional regions within Costco, Walmart and Safeway stores we continue to expect further positive updates from here.

INVESTMENT PHILOSOPHY

INVESTMENT OBJECTIVE

The Fund seeks to provide Unitholders with a concentrated exposure to a high quality portfolio of listed companies outside the S&P/ASX 50. Employing an extensive investment process that combines a rigorous company visitation schedule and fundamental bottom-up analysis, the Fund aims to identify businesses operating within structural growth sectors with the ability to meaningfully grow and compound earnings over time. The Fund aims to generate long-term returns in excess of the Benchmark (after fees and before tax) and provide consistent, sustainable returns for Unitholders.

INVESTMENT PROCESS

Ophir employs a fundamental, bottom-up research approach aimed at identifying businesses with the ability to meaningfully grow and compound earnings over time. Typically, the investment process will look to uncover businesses that are operating within, or about to enter, a period of structural growth and are generating cash or have a clearly identifiable pathway toward free cash flow generation. In order to identify these opportunities, the Ophir investment team spend a considerable amount of time understanding the quality of the business and the environment in which it operates.

ABOUT OPHIR ASSET MANAGEMENT

Ophir Asset Management is a specialist small and mid-cap equities investment manager established by founders Andrew Mitchell and Steven Ng in 2012. The business currently manages approximately $1.0bn in capital across two investment strategies on behalf of institutional superannuation funds, family offices, private wealth groups and individual investors. The investment team comprises 5 investment professionals drawn from a diverse range of backgrounds working across all Ophir funds.

ABOUT THE PORTFOLIO MANAGERS

Senior Portfolio Managers Andrew Mitchell and Steven Ng co-founded Ophir Asset Management in 2012 after previously managing capital together at Paradice Investment Management. Under their stewardship, the fund managed by Andrew at Steven at Paradice was the top performing equities fund in Australia from 2007-2011 versus the fund manager surveys (inclusive of the GFC). At Ophir, Andrew and Steven are Senior Portfolio Managers for the Ophir Opportunities Fund (having returned 23.6% p.a. since inception after fees) and the Ophir High Conviction Fund (returning 17.0% p.a. since inception after fees).

KEY INVESTOR CONTACTS

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