PORTFOLIO UPDATE

May 2017

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From the Directors

Australian equity markets behaved as we expected in May. Australian banks were sold off aggressively - resulting in the ASX 20 price index being down -5.76% - while the broader market, represented by the ASX 200, was negative 3.38%. The Small Ordinaries fared slightly better but was still down at -2.10%. Overall, global equity markets were stronger with currency having little impact for local investors in the month of May.

Both of TAMIM's Australian equity **value** solutions have performed well over the past few months and we continue to hold our view that the large end of the Australian equity market looks vulnerable across resources, banks and retail. We are once again experiencing selling pressure across parts of the small cap segment of the Australian equity market. There are a number of small cap managers that are experiencing outflows from their portfolios. This typically results in the price of their investments going down, TAMIM will normally use this opportunity to add to client portfolios. The downside, however, is short term weakness in returns.

This month Guy Carson, head of TAMIM's Australian Value strategies, was again published in The Australian, you can read his article about the potential for recession in Australia by clicking **here**. We are always open to discussion and we wish you successful investing.

Yours Sincerely,

Darren Katz,
Joint Managing Director

Jeff Taitz,
Joint Managing Director

TAMIM

TAMIM Australian Equity All Cap Value IMA

The Australian equity market sold off during May lagging major markets around the globe. The main driver was the federal budget and the announcement of the bank levy. This saw the share prices of the big four banks down significantly with returns of between -8.6% and -12.2% for the month. Whilst we didn't expect the bank levy, we had written recently about the risk of greater regulation in our article "Australian Banks: The death of a 25 year bull market". This is part of a greater trend and we expect further changes from APRA in the months ahead. Elsewhere, commodity prices weighed on the Small Ords with Iron Ore down 19% for the month. Weak retail conditions also persist with downgrades from AP Eagers and Automotive Holdings Group. Despite all the challenges, the underlying portfolio managed a solid month up close to 1% against the backdrop of a market down over 2.5%. The performance was primarily due to contributions from Melbourne IT (+18%) and Gentrack (+7%).

Portfolio News

The best performing stock in the portfolio over the month was **Melbourne IT** (+18%). This was on the back of the capital raising and the acquisition of WME Group. The acquisition is earnings positive and continues what has been a successful turnaround strategy from the company. Three years ago the company saw its core domain business in decline and needed to diversify. In response to this the company expanded its more diversified services division through acquisition. The domain business now represents c. 20% of its earnings and the services division is showing strong growth both organically and through further acquisition.

Another company that continues to perform well is **Gentrack** (+7%) and later in the month the company reported its first half result. The result was very strong with Revenue up 24% and NPAT up 46%. Guidance for the full year was a little below market expectations primarily due to the timing of earnings within the recently acquired Junifer Systems which had been running to a different financial year. This ultimately sets Gentrack up for a strong FY18 in addition to the growth seen this year.

One of the laggards in the portfolio was **Adacel Technologies** (-8%). The company downgraded FY17 earnings due to the award of several projects being delayed. The company remains profitable, has a net cash balance sheet and in response to the downgrade announced a share buyback to show conviction in its strong future. We continue to hold the company albeit it at a reduced position.

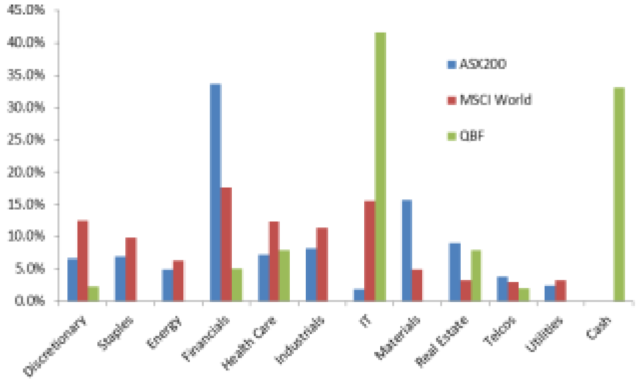
The Portfolio

The portfolio is currently invested in 17 companies. The cash level is currently 33%. The positions above 5% are shown below. Of the larger positions, we reduced our exposure to Gentrack and IMF Bentham due to recent rallies. We continue to hold both companies

Gentrack Group	**7.3%**
Melbourne IT	**6.4%**
Data#3	**5.6%**
Altium	**5.2%**
IMF Bentham	**5.1%**
Mitula Group	**5.1%**
Other Positions	**32.2%**
Cash	**33.1%**

Sector Positioning

The portfolio maintains a strong overweight to the IT sector with other exposures in Healthcare, REITs, Financials and Telcos.



Guy Carson,
Portfolio Manager

TAMIM Australian Equity Small Cap IMA

The Portfolio

The disappointing return for the underlying portfolio during May can be broken down into two components.

Approximately half the negative performance is attributable to a holding in Murray River Organics (ASX:MRG) which saw its share price react savagely to two disappointing earnings downgrades during the month. At the time of our investment into MRG, we were attracted to MRG's position as a leading global producer of organic produce, a key supplier of organic products to Australian supermarket chains, and an owner of high quality Australian farmland. In hindsight, we misjudged the agricultural risk and MRG's earnings sensitivity to a poor harvest, as well as having a too optimistic view on Management's ability to execute a number of initiatives they were attempting. We substantially sold our position prior to MRG's second earnings downgrade, thus limiting our losses.

The balance of the negative performance came from holdings which suffered from a lack of news-flow, poor liquidity and general lack of buying interest in the micro-cap and small cap space. This included some key holdings such as ASX:ZNT, ASX:GAP and ASX:MNY. We have used this weakness as an opportunity to increase our holdings in a number of high conviction portfolio positions.

We believe the underlying fundamentals and investment thesis of our portfolio holdings remain strong, and the valuation metrics are compelling.

We acknowledge the under-performance of the portfolio since the start of the calendar year and look forward to an improved performance over the coming months. Despite the challenges in the small cap space and large rotation out of small caps in recent months, the portfolio remains up over 17% this financial year to date. The small cap space offers some very compelling investment opportunities, which will drive renewed interest and improved sentiment over time.

Whilst there was limited news flow across the portfolio during the month, one holding that reported positive news was Konekt Limited (ASX:KKT). The Konekt article can be found by clicking here.

A selection of top portfolio positions as at 31 May 2017 (in no particular order):

ASX**: JYC**
m/c: $47m
Outlook: "substantial growth opportunities"

ASX**: FID**
m/c: $131m
Outlook: "double digit earnings growth"

ASX**: PGC**
m/c: $121m
Outlook: "double digit earnings growth"

ASX**: PNC**
m/c: $126m
Outlook: "high quality, cautious and disciplined growth"

ASX: **ZNT**
m/c: $40m
Outlook: "confirm EBITDA guidance"

TAMIM Australian Equity Income IMA

Market Commentary

The Australian equity market returned -2.8% in May, after the announcement of a bank levy and uninspiring profit results precipitated a 10% sell-off in the major banks. Excluding the banks, the market was approximately flat for the month.

The banks reported flat to negative revenue growth for the half year, excluding markets and trading, with CBA outperforming peers on this measure. This was disappointing given mortgage repricing activity, while the banks pointed to a greater repricing benefit in the second half.

Improving cost control was one positive aspect and bad debts also remained at very low levels. This was overshadowed by the Government's bank levy, which is expected to impact earnings by approximately -2%, assuming approximately half of the cost can be passed on to customers.

International equity markets were largely positive in May, with the S&P500 gaining 1.2%, the FTSE100 up 4.4%, the German Dax up 1.4%, the Nikkei 225 up 2.4% and the NZX50 up 0.5%, while the Shanghai composite declined 1.2%.

Across Australian industry sectors, telecommunications +3.4%, energy +2.0% and utilities +1.0% led gains, while banks -9.8%, industrials -3.5% and diversified financials -1.6% were the worst performing sectors.

Portfolio Commentary

Company share price performance during the month was more diverse than the recent norm with the bank sector particularly weak. National Australia Bank (NAB, 2% weight) was the best performer declining -8.5%. While ANZ was the worst (ANZ, 1.9% weight) dropping -12.5%. We remain underweight the banks as a group, however we added to our position in all four banks following the substantial price decline. We are happy to hold a larger but still much smaller than benchmark position as a result of their strong income (high dividend) generating characteristics.

Macquarie Atlas Roads (**MQA**, 5.2% weight) returned 9.6% in May, benefiting from a 19bp reduction in the Australian Government 10-year bond yield and a 4.0% strengthening of the euro relative to the Australian dollar. Approximately 85% of MQA's forecast earnings are derived from the APRR toll road in the east of France.

Spark Infrastructure (**SKI**, 2.4% weight) returned 8.4%, benefitting from investors reinvesting funds freed up from the completion of the takeover of Duet (**DUE**) by Cheung Kong Infrastructure (HK). The takeover reinforced the value of these scarce assets.

Automotive Holdings Group (**AHG,** 0.9% weight) returned -21.2% after reducing FY2017 net profit guidance by 9% as a result of softer vehicle industry sales, particularly in WA, and tighter consumer credit conditions. With the company continuing to target operational improvements and given upside relative to our valuation, the portfolio has maintained its position.

Sydney Airport (**SYD**, 2.0% weight) returned 8.0% following the announcement that the company would not participate in the development of Sydney's second airport at Badgery's Creek.

Overall the market rewarded those stocks who can deliver stable earnings. A range of companies have warned of weaker than expected conditions in the May/June "confession season" prior the end of the fiscal year. We continue to look for defensible earnings at the right share price as we build a portfolio of high quality companies.

Scott Maddock,
Portfolio Manger

TAMIM Global Equity High Conviction IMA

The underlying strategy declined in May which was a poor result given that equity markets rose. This is not the worst relative drawdown in the strategy's history but we are investigating the reasons.

We expect to bounce back but are not passively waiting!

Preliminary work indicates that our stock model is suggesting many attractive stocks which perform well but our 'fundamental" choices amongst these has been the problem. Macys, Cisco and Japan Airlines all detracted significantly.

The spread between the performance of growth and value stocks is now very wide and we have favoured a more significant value bias since the middle of 2016.

It is more likely that the risk premium in value stocks is now meaningfully higher and worth capturing.

The equity market, especially in the USA, is becoming alarmingly narrow with a small group of stocks rising significantly while the majority mark time or fall. The "Sexy Six" (Amazon, Apple, Facebook, Google, Microsoft and Netflix) have risen significantly ahead of the rest of the USA market. We continue to own Apple.

Market and Portfolio Review

Equity markets were stronger in May with the MSCI World Value Weighted index rising around 2.0% in AUD terms. In AUD terms the High Conviction Strategy performed poorly, declining 1.0% in May.

The market during the period was again largely driven by growth and quality, with the broader MSCI World index rising 2.6%. We continue to believe that value will win out in the long run as many growth stocks are expensive.

Since inception the portfolio returns are stronger with total return of 180% compared to the Value Weighted index of 130%.

Stock selection in several stocks detracted with Macy's, Cisco and Japan Airlines especially disappointing. We believe this is a short-term issue. Investors are focussing on revenue 'shortfalls' without regard to the fact that it's profitable revenue and sensible capital allocation that matter more than simple revenue growth.

Market Outlook

We now have a more significant value bias in the portfolio than we have for a while, although we have been value oriented since inception.

The spread between the performance of growth and value stocks is now the widest it has been since 1995. It is more likely that the risk premium in value stocks is now meaningfully higher and worth capturing.

The equity market, especially in the USA, is becoming alarmingly narrow with a small group of stocks rising significantly while the majority mark time or fall. The Sexy Six (Amazon, Apple, Facebook, Google, Microsoft and Netflix) have risen significantly ahead of the rest of the USA market. We continue to own Apple.

You should never drive by looking only in the rear view mirror.

Oil prices retreated, as did long term interest rates, and the political backdrop remains 'exciting'. The UK general election takes place in early June and we expect the incumbent party to be returned which should remove some uncertainty.

We remain fully invested in the model portfolio and unhedged for AUD based investors.

Robert Swift,
Portfolio Manager

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