



Ophir Asset Management
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SYDNEY NSW 2000

Dear Fellow Investors,

Welcome to the **February 2018** Ophir Letter to Investors – thank you for investing alongside us for the long term.

Month in Review

February 2018 marked the beginning of the ‘Year of the Dog’ for the Chinese Lunar New Year and for Australian equity market investors the proverbial tail has begun to finally wag, at least in a relative sense. After shrugging off what was ultimately a short, yet fairly pronounced, period of global equity market volatility at the beginning of the month, Australian equity markets responded favourably to a half-yearly earnings season that provided a broadly positive outlook for the Australian corporate sector. Inclusive of dividends, the S&P/ASX 200 finished February +0.4% - the only single country index in the region to finish in the green - while the Small Ordinaries Index finished the month flat.

	1 month	6 Months	1 Year	5 year p.a.	Inception p.a.
Ophir Opportunities Fund [^]	1.7%	23.6%	39.4%	30.4% p.a.	38.2% p.a.
Benchmark*	0.0%	14.6%	20.8%	6.2% p.a.	8.2% p.a.
Value Add (Gross)	1.7%	9.0%	18.6%	24.2% p.a.	30.0% p.a.
Fund Return (Net)	1.6%	22.8%	37.6%	23.6% p.a.	30.1% p.a.

* S&P/ASX Small Ordinaries Accumulation Index (XSOAI)

	1 month	6 Months	1 Year	2 Year p.a.	Inception p.a.
Ophir High Conviction Fund [^]	4.7%	25.2%	39.5%	23.5% p.a.	33.1% p.a.
Benchmark*	0.5%	13.8%	21.0%	6.8% p.a.	15.7% p.a.
Value Add (Gross)	4.3%	11.5%	18.6%	16.6% p.a.	17.4% p.a.
Fund Return (Net)	3.8%	23.3%	36.4%	21.1% p.a.	26.9% p.a.

* 50% S&P/ASX Small Ordinaries Accumulation Index (XSOAI), 50% S&P/ASX Midcap 50 Accumulation Index (XMDAI)

Reporting season always proves to be a fascinating, albeit hectic, period for the investment team as volumes of half-yearly company updates are provided en masse to the ASX over a concentrated three-week period. It is a unique opportunity for us to analyse a wide ranging cross section of corporate Australia and gain real-time updates from senior executive teams regarding the health, outlook and growth options for their respective companies and industry sectors. Across the Ophir investment team this month, we had the pleasure of meeting with 82 different company management teams in one-on-one settings (including all current portfolio investments that reported over the month), in addition to attending a further 105 company updates via institutional group meetings.

We’re pleased to report solid performance across both Ophir Funds over the period, **the Ophir Opportunities Fund adding +1.7% over the month, while the Ophir High Conviction Fund added +4.7%**. While the vagaries of month-to-month reporting should never be the focus for investment management teams, we do gain a certain level of satisfaction in delivering reasonable returns through the bi-annual reporting periods. One, because it provides us with confirmation that the underlying stock selection process is continuing to deliver us with favourable outcomes (i.e. correctly identifying businesses with the capacity to grow earnings and avoiding those businesses

likely to incur loss of capital); and two, as a good reporting period often sets up the portfolio well for continued performance over the following months.

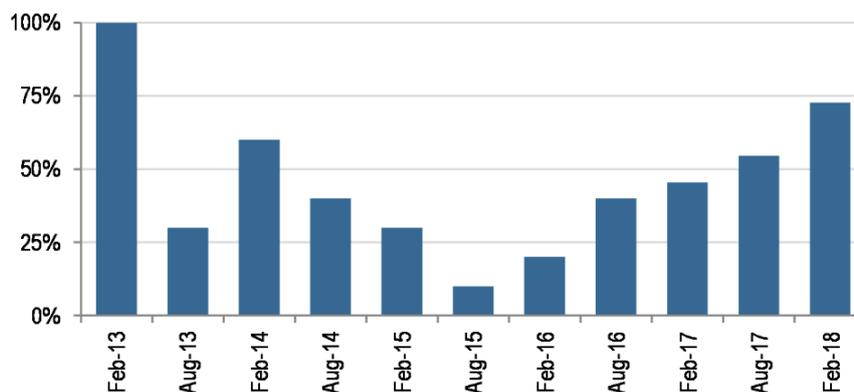
This positive performance tailwind is typically generated by the inevitable recycling of capital within the market away from businesses that have seen negative earnings revisions and into those with more favourable earnings outlooks (or, more simply, the market “selling the losers and buying the winners”). Quite simply, if one is fortunate enough to be favourably positioned in a good number of businesses that report well, then historically overall portfolio performance tends to benefit over the following months as share prices respond to the increasing demand from the broader market.

With that in mind, we’re happy that both portfolios are likely well positioned to benefit from those tailwinds over the coming months. Looking across the Ophir Fund’s as an amalgamated group, we entered February with a total of 57 investments across both portfolios, 42 of which provided half-yearly earnings updates that were previously unguided and/or provided new information to the market. Across this collection of businesses, **the funds were exposed to twelve companies that upgraded earnings guidance and just one company that downgraded.** These are pleasing results and we’re happy that the investment process continues to deliver favourable overall outcomes and the portfolios remain well positioned for the months ahead.

The performance of the High Conviction Fund this month is worthy of some mention given it provides a sound example of the merits of constructing more concentrated portfolio positions within businesses where one has a high level of conviction. For investment management teams, correctly identifying a business with the ability to revise earnings positively is often only half the battle – one must also ensure they own a meaningful amount of the business in their portfolio in order to ensure a positive impact on overall returns. As a concentrated fund that only owns 15-30 stock positions at any one time, the High Conviction Fund’s objective is to identify opportunities in which the investment team has a high level of conviction and duly allocate a sizeable amount of capital into these names. Pleasingly, these portfolio of investments delivered well this month, benefiting materially from a number of concentrated positions in companies that delivered highly favourable updates, including **A2 Milk (A2M)**, **Seven Group Holdings (SGH)** and **Flight Centre (FLT)** – all three of which sat within the top five weightings of the portfolio at the beginning of the month.

As a general summation of the entire reporting period, the net takeaways from the reporting period have been fairly positive. Overall earnings growth remains solid, albeit with some signs of cost pressures beginning to impact margins, whilst top line revenue growth across the market as a whole averaged around +6%. In a sign of improving overall corporate health, of the businesses that reported earnings numbers in February across the ASX 200, only 4% reported a loss for 1H18 (the lowest level since 2007). In an equally positive sign, 73% of the ASX 200 GIC industry sectors registered positive overall earnings revisions (the highest level since February 2013), indicating an increasing breadth of earnings growth across most market sectors.

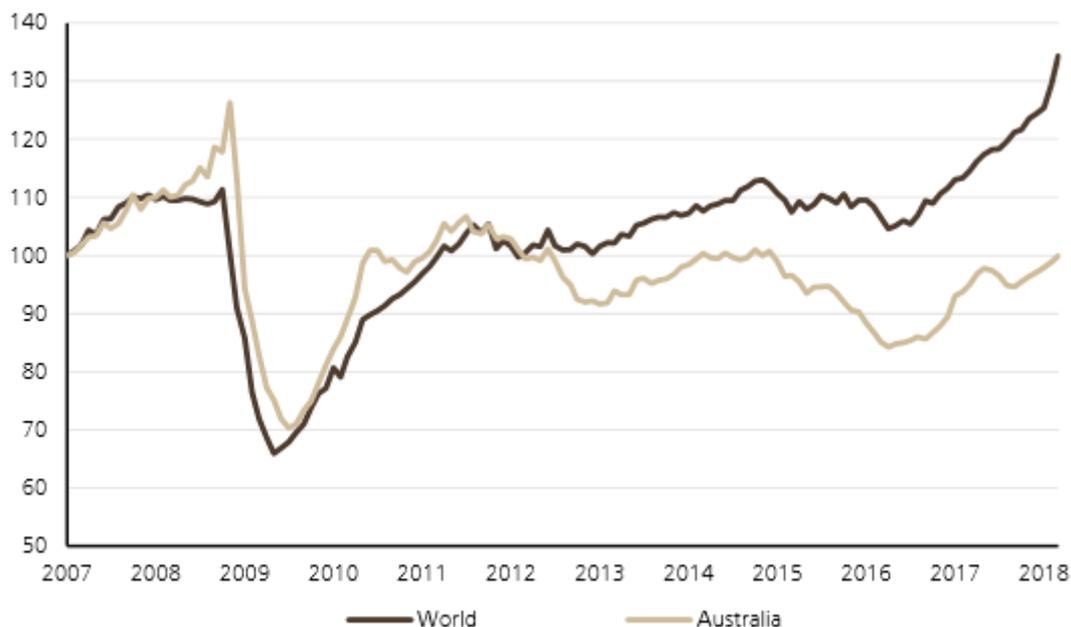
Proportion of ASX 200 GIC’s Sector’s Upgrading (1H18 Reporting Season)



At a whole-of-market level, **growth forecasts for FY18 have remained fairly resilient following the results period**, a phenomenon that can be somewhat of an anomaly for the Australian market. More often than not, the wider sell side analyst community tend to start each financial year with reasonably elevated earnings expectations that then ultimately drift lower as the year progresses. Often a large proportion of that adjustment occurs post the February results, however broader consensus estimates for FY18 have so far remained relatively stable. Perhaps as confirmation of that conviction, the proportion of companies that saw their overall analyst recommendation change following their earnings release was the lowest amount in six years. This might also suggest that market positioning, at least across the large caps, has most likely stayed equally static.

Unsurprisingly, **locally-listed businesses exposed to offshore markets again proved the big winners** through the season as the global economy continues to power ahead at a rate considerably higher than the current domestic experience. While overall profit growth across the broader Australian market will likely come in around +6-7% for FY18 (i.e. slightly above longer term averages), excluding resources the number falls to a more miserly +3% for the year. When one considers current global profit growth expectations sit around 12-14% for the year, the relative underperformance of the Australian market versus global peers continues to be striking. With an index dominated by older world businesses that, as yet, are broadly underexposed to the growth across the newer world businesses and sectors, this relative underperformance is an unfortunate reality that may continue to face Australian larger cap investors for some time.

Australia Expected EPS Relative to Global Equities



Source: UBS Investment Research

In the smaller cap end of the market, results were broadly mixed with solid earnings performances coming from a wide range of fairly niche industry sectors, many of which aren't overly well represented within the top ASX 50 yet are seeing (in some cases) some stellar growth outcomes. **In this month's 'Strategy Notes' we'll discuss a number of these growth sectors (and the companies exposed to them) and our overall thoughts on the reporting season as a whole.**

Ophir High Conviction Fund - To Soft Close This Month

As regular readers of these Letters will be duly aware, the Ophir High Conviction Fund – our only Fund currently accepting new investments – has been approaching a level where we feel it is appropriate to close off the fund to additional investment capital.

The purpose of closing the Fund is ultimately to ensure the future performance of the strategy is not impacted by its size and will also ensure we are able to leave a small amount of remaining capacity in the Fund for existing investors, adviser groups and wrap platform clients that have supported the business for some time.

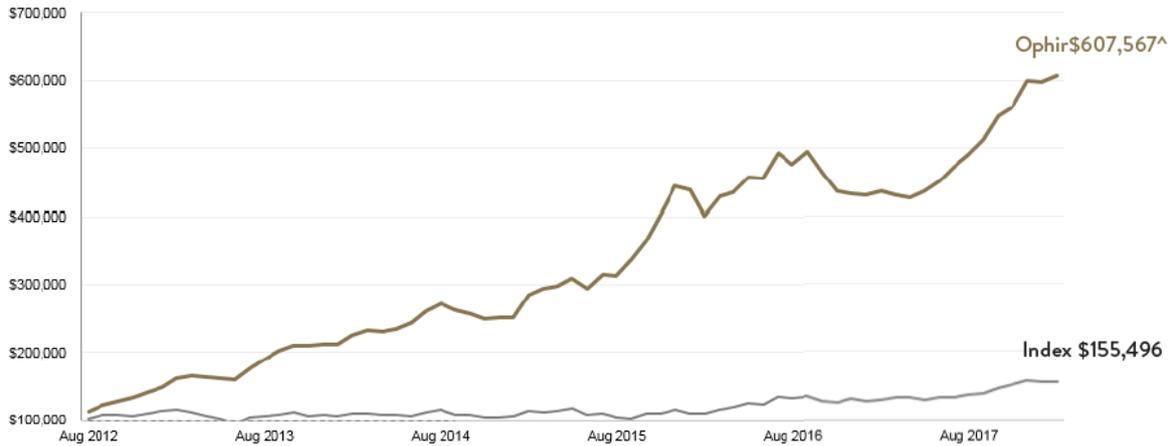
Through a combination of recent inflows and strong Fund performance, we are advising that the Ophir High Conviction Fund will be soft closing at the end of this month, with all new fund applications (and monies) required to be submitted to Link Fund Solutions by Friday 30th March.

Existing investors will receive an additional update directly from us to provide some more detail around the fund closure and their ability to continue to add to their existing investments through the Soft Close period.

All individual existing investors and adviser partners are more than welcome to contact Ophir Investment Director Rob Saunders on (02) 8188 0397 or rob.saunders@ophiram.com to discuss in more detail. We thank everyone for their continued support and very much look forward to continuing to provide strong returns on your investment capital.

The Ophir Opportunities Fund

Growth of A\$100,000 since Inception (gross)



The **Ophir Opportunities Fund** returned +1.7% for the month, outperforming the benchmark by 1.7%. Since inception, the Fund has returned +507.5%, outperforming the benchmark by +452.1%.

	1 Month	1 Year	5 Year (p.a.)	Inception (p.a.)	Since Inception
Ophir Opportunities Fund (Gross)	1.7%	39.4%	30.4%p.a.	38.2% p.a.	507.5%
Benchmark*	0.0%	20.8%	6.2%p.a.	8.2% p.a.	55.5%
Gross Value Add	1.7%	18.6%	24.2%p.a.	30.0% p.a.	452.1%
Net Fund Return	1.6%	37.6%	23.6%p.a.	30.1% p.a.	334.6%

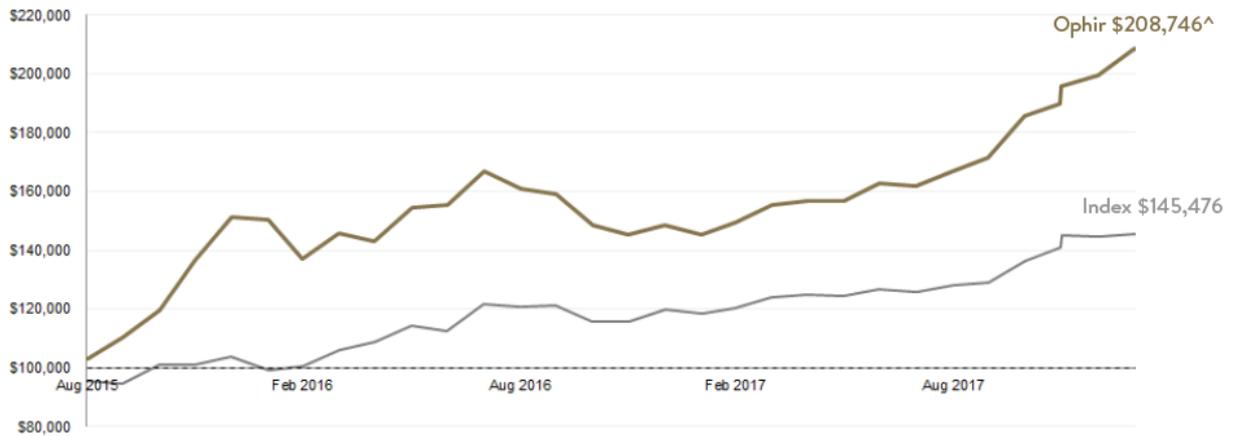
* S&P/ASX Small Ordinaries Accumulation Index (XSOAI)

	Buy Price	Mid Price	Exit Price
February 2018 Unit Price – Opportunities Fund	2.8499	2.8399	2.8300

Key contributors to the Opportunities Fund performance this month included **The A2 Milk Company Limited (A2M)**, **Redbubble Limited (RBL)** and **Service Stream (SSM)**. Key detractors included **EML Payments Ltd (EML)**, **Motorcycle Holdings (MTO)** and **Zip Co Ltd (Z1P)**.

The Ophir High Conviction Fund

Growth of A\$100,000 since Inception (gross)



The **Ophir High Conviction Fund** returned +4.7% for the month, outperforming the benchmark by 4.3%. Since inception, the Fund has returned +108.7%, outperforming the benchmark by +63.3%.

	1 Month	1 Year	2 Year(p.a.)	Inception (p.a.)	Since Inception
Ophir High Conviction Fund (Gross)	4.7%	39.5%	23.5%p.a.	33.1% p.a.	108.7%
Benchmark*	0.5%	21.0%	6.8%p.a.	15.7% p.a.	45.5%
Gross Value Add	4.3%	18.6%	16.6%p.a.	17.4% p.a.	63.3%
Net Fund Return	3.8%	36.4%	21.1%p.a.	26.9% p.a.	84.7%

* 50% S&P/ASX Small Ordinaries Accumulation Index (XSOA1), 50% S&P/ASX Midcap 50 Accumulation Index (XMDAI)

	Buy Price	Mid Price	Exit Price
28 February 2018 Unit Price – HCF	1.8383	1.8328	1.8273

Key contributors to the High Conviction Fund performance this month included **The A2 Milk Company Limited (A2M)**, **Seven Group Holdings (SVW)** and **IDP Education Ltd (IEL)**. Key detractors included **Premier Investments (PMV)**, **Pushpay Holdings Ltd (PPH)** and **SG Fleet Group Ltd (SGF)**.

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