SGH ICE

31 August 2017

SG HISCOCK & COMPANY

Fact Sheet

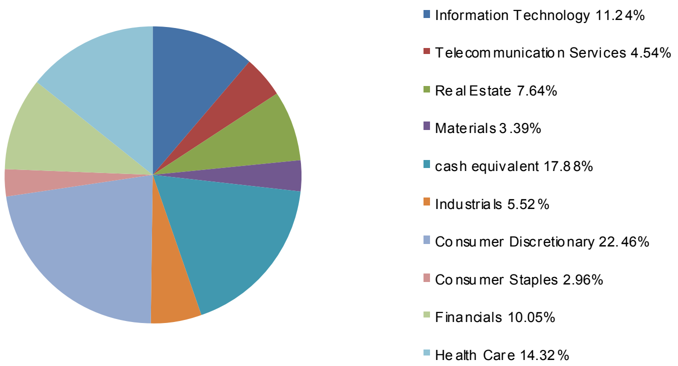
Investment objective	Aims to deliver superior medium to long term returns by investing in listed companies which possess a sustainable competitive edge. Companies can create that by owning/operating assets that are difficult to replicate. The Investment Manager believes that key intangible assets (such as Brands, Licenses, Patents, Logistical capability, a Captive client base) are the most difficult to replicate and that these key assets enable companies to entrench their products/services in the marketplace.		
Investments held	A portfolio of approximately 30-50 predominantly ASX listed securities (a minimum of 15 and generally no more than 80); cash and derivatives.		
Investment Manager	SG Hiscock & Company		
Commencement	13 February 2006		
APIR	ETL0062AU	**mFund Product Code**	SHF02
Minimum initial investment	$20,000	**Buy Spread**	+0.35%
Management costs[1]	1.180% p.a.	**Sell Spread**	-0.35%
Performance Fee[2]	15.375%	**Pool size**	$637.36 million

Unit Prices	Application	Net Asset Value	Withdrawal
31 August 2017	$ 1.9636	$ 1.9568	$ 1.9500

Performance as at 31 August 2017[3]	1 mth %	3 mths %	6 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	Inception % p.a.
Total Net Return	1.41	2.11	7.41	-0.33	8.59	14.61	11.14
S&P/ASX Smallcap Industrial Index	1.68	3.93	5.85	1.57	7.00	10.67	3.69
S&P/ASX 300 Accum. Industrials Index	-0.19	-0.43	1.27	6.64	6.60	12.74	6.73
S&P/ASX 300 Accumulation Index	0.75	0.99	2.43	9.54	5.16	10.41	5.77

Distribution Period	31-Dec-15	30-Jun-16	31-Dec-16	30-Jun-17
Distribution rate (cents per unit)	0.6485	11.0518	0.7943	1.3505

Asset allocation as at 31 August 2017



Top 5 holdings as at 31 August 2017
Carsales.com Ltd
Ooh! Media Ltd
Janus Henderson Group- GDI
MYOB Group Limited
Bapcor Limited

Top 5 holdings represent 16.70% of total fund.

1. Includes estimated GST payable, after taking into account Reduced Input Tax Credits ("RITC").
2. A performance fee of 15.375 (inclusive of GST and an estimate of RITC) of any performance in excess of the performance hurdle (the daily percentage movement in the S&P/ASX 300 Accumulation Index plus 1.20 p.a. calculated on a daily basis) may also be payable.
3. Performance: Distribution Return is the return due to distributions paid by the Fund, Growth Return is the return due to changes in initial capital value of the Fund, Total Net Return is the Fund return after the deduction of ongoing fees and expenses and assumes the reinvestment of all distributions.

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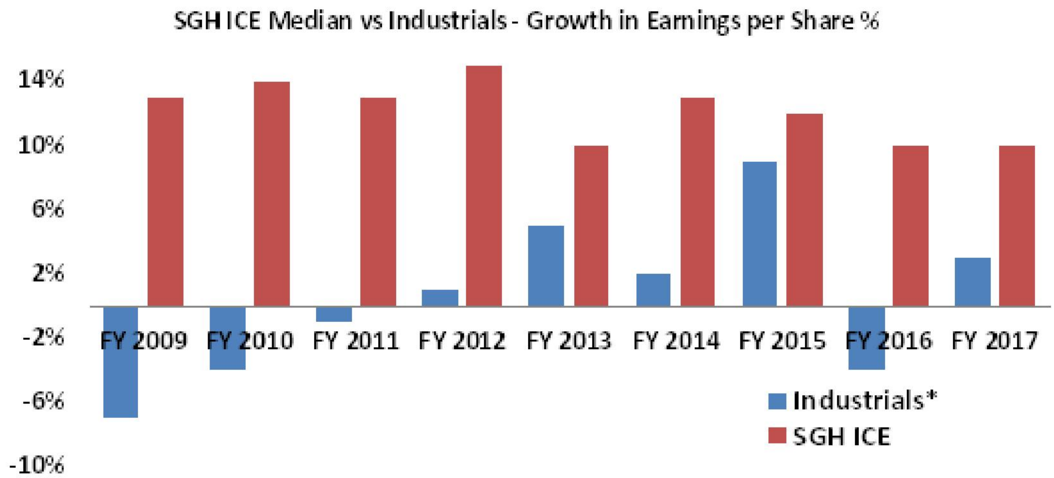
Commentary

The main event for August was the FY 2017 reporting season. With results now in, we are pleased to report median growth in earnings per share for companies in the ICE fund was a strong +10%, continuing the trend of ICE portfolio companies delivering 'more certain earnings growth'. This compared favourably against the +3% earnings growth for ASX Industrials (ex Banks and Property).



**Source: Macquarie*

After delivering an –11% fall in earnings in FY 16, All Companies (including Resources) reported +16% earnings growth in FY17. Consensus is currently forecasting a return to a more moderate +5% in FY 2018.

Result highlights of reporting season included oOh!media which delivered +27% earnings on +18% revenue growth. Outdoor media continues to take an increasing share of the overall media pie through its ability to provide both broad audience reach and location based advertising campaigns. Digital conversions have been a key facilitator of advertiser interest (in addition to the fragmentation of media) and over half of oOh's revenues now come from digital screens. While many more sites can still be converted to digital, oOh!media is preparing for the next wave of digitisation with investment in data capability in order to help advertisers achieve more targeted campaigns.

While Bapcor's +36% earnings growth was assisted by the integration of acquisitions, its core Burson Trade business still grew revenues +11% and EBITDA +22% on consistent underlying market growth (3-4%) and store rollout. The performance of Bapcor's Retail business was driven by improvement of the offering post acquisition and a move to increase company owned stores with some rationalisation of the franchise network. Bapcor is also expanding its wholesale offering which supports its Trade & Retail businesses in providing a competitive product offering.

As the country's leading mortgage aggregator, AFG continues to attract additional mortgage brokers due to its market leading technology platform and breadth of product offering (assets that are difficult to replicate). Earnings grew 34%, significantly outperforming its peers, on strong growth in higher margin products.

MYOB delivered another consistent result with +10% earnings growth. MYOB's brand recognition allows it to drive strong growth in online products by tapping into a new customer segment as well as upgrading its sticky user base to current technology. The company has recently made changes to their R&D function which will augment their ability to roll-out new features that underpin their mid-single digit price increases and accelerate the move online.

In small-mid caps there are always some results that don't go according to plan. We had Iress on watch heading into reporting season based on slow progress on capitalising on the market opportunity in the UK, and consequently exited the position on a weak result (-6% earnings decline in constant currency). Trademe's FY17 result was a solid +12% earnings growth as expected but the company also guided to a higher than expected need for increased investment in FY18 to combat increased competition. This reduced earnings growth forecasts so we commensurately reduced the position in this stock reflecting the lower IRR.

Key contributors during the month were A2 Milk (see below), Carsales (+7% earnings growth), oOh!media, Sydney

Airport (+8% earnings growth) and MYOB. Key detractors were Trade Me, Iselect (+26% earnings growth but below top end of guidance range) and Iress.

Market Comment

It seems investors have become well aware of the shortage of earnings growth in the overall Industrials market and their short term response has been paying up for high earnings growth via (1) potential cyclical/lower quality profit turnarounds and (2) companies with excellent earnings growth prospects, irrespective of valuation.

Analysis of the Small Industrials in August shows where investors are focused short term. Within that index 26 stocks (29 including listed property trusts) delivered returns >10% over August. 9 of the 26 were cyclical/lower quality companies and another 7 were very high growth companies with very high valuations. The FY17 PE ratios for these 7 companies range from 27x to 99x at time of writing. This compares to the FY17 PE ratio of the Industrials ex Financials of 18x. Of the remaining companies, 1 we own and the balance is a miscellaneous group where we have question marks about the sustainability of earnings growth going forward.

ICE continues to pursue the 'quality industrial franchise at the right price' strategy that has stood the test of time – sticking to our quality and valuation disciplines. As the above analysis shows, this means our companies have been a bit in the shade of late but reporting season demonstrated the ICE company's earnings power remains strong and the ICE median forward PE premium to the Industrials is 8%, at the lower end of the typical range. We believe this will in due course be recognised by the market as it has many times before—as the strong medium to long term returns attest.

Some evidence of that view playing out in a stock specific sense is A2 Milk. We commented in February that the A2 result was the most extreme example of dislocation between the stockmarket and underlying company operating performance. At the time, A2 had delivered one of the standout (and above consensus) results of the H1 FY17 result season, yet the share price actually fell –3% on result day. The share price has since taken off and is now double what it was 6 months ago, assisted by another strong result for H2 FY17 (20% above H1 despite supply constraints for much of H2). This is obviously an extreme example, both in terms of magnitude and speed, but is proof of the adage that in the short term the market is a voting machine but in the long term it is a weighing machine.

Portfolio Activity

Reporting season portfolio activity included taking profits in A2 Milk, reducing Trade Me and Orica, initiating in Ramsay, exiting Iress, and building positions in an additional three companies.

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