WENTWORTH WILLIAMSON

Quarter ending 31 December 2017

As you are aware, the objective of the Wentworth Williamson Fund (the Fund) is to generate superior returns to our competitors over the long term by acquiring a select portfolio of value-driven investments. We aim to protect our clients' principal while growing capital well above the prevailing cash rate over the medium to long term.

A REMINDER - INVESTMENT APPROACH

The prices of shares tend to vary far more than the value of the underlying businesses in the short term. Some of the factors that contribute to this are:

- Economic sentiment
- General market sentiment towards equity investments as a category
- Management changes
- Country-specific issues
- Market's view that the business model is broken (at least in the short term) or conversely overly optimistic expectations; and
- Lack of sell-side research due to size or free float in the shares of the company or conversely the 'follow the pack' mentality often driven by mainstream, widely read analysis and research

We aim to invest in companies that, in our view, fall below their underlying value (often as we have a contrary view to the market for the reasons mentioned) and sell when the price rises above our assessment of fair value.

The key aspect of our investment process is determining the underlying or intrinsic value of the businesses. We therefore spend a great deal of time developing differentiated information that helps us determine the intrinsic value of a target company. The process involves rigorous research and analysis of the industry and competitors, in order to construct a detailed picture of the dynamics of the market and investment being reviewed.

By not limiting ourselves to any market capitalisation size or sector and by allocating more time to research and investing (rather than trading) we believe this strategy gives us a structural competitive advantage to generate returns in excess of our benchmark.

The current composition of the portfolio is set out in the Appendix on page 5.

Returns (%)	WWF Fund	S&P/ASX 300 Accumulation Index	Relative Performance
Cumulative			
Since inception	63.0%	37.7%	**25.3%**
Annualised			
Since inception	12.2%	7.8%	**4.4%**
Latest 4 years	13.0%	7.9%	**4.1%**
Latest 3 years	13.9%	9.0%	**4.9%**
Latest 2 years	10.8%	11.9%	**-1.1%**
Latest 1 year	6.6%	11.9%	**-5.3%**

Returns are net of all fees, include income, assume reinvestment of distributions and exclude any spreads that might be payable on some transactions. Inception date is 30 September 2013.

Over the past 18 months there was unusually high activity in the portfolio as many our investments reached maturity after a holding period of approximately 3-4 years. We exited key investments in UGL Limited, Broadspectrum, Event Hospitality & Entertainment Limited, Collins Foods Limited, Grays eCommerce Group/Eclipx Group, WorleyParsons, Nuplex Industries and Royal Wolf Holdings, realising considerable capital gains for our unit holders in each case. It therefore became necessary to refresh our portfolio with new businesses that we believe will generate significant capital gains over the next few years even if, as we expect, the backdrop becomes more challenging for our consumer driven economy with a goal of outperforming market peers over the long term.

Today our top five positions of GCS Limited (GCS), CSG Limited (CSV), ERM Power Limited (EPW), Austal Limited (ASB) and TPI Enterprises (TPI) were all seeded in the portfolio within the past year and a half. These investments are all in their early stages and typically it takes three to four years for our investment thesis to come to fruition. In previous quarterly updates we elaborated on our investment thesis for Austal (December 2016), CSG (March 2017) and GCS (September 2017). In this communication, we expand on our thinking behind another business in our portfolio with revenues not dependent on a heavily indebted consumer, ERM Power Limited.

ERM Power Limited (EPW)

We believe EPW is misunderstood by the market and is often placed in the 'too hard to value' basket which, coupled with a relatively small market capitalisation of only $350m, has resulted in a share price that in our opinion significantly undervalues the business and underlying assets. The company has 3 key characteristics that excite us about its future:

1. A stable best in class Australian electricity retailing business selling to the Commercial and Industrial (C&I) sector;
2. A significant growth opportunity in the US that is at an inflection point and will generate significant profits in the coming years;
3. An asset backing with the estimated replacement value exceeding the current market capitalisation.

Most of the current earnings are generated by the Australian energy retailing business that specialises in the C&I sector. Since entering the market in 2006, EPW has grown rapidly and now has the second highest market share with best in class customer service levels. The year 2016 marked the 6th consecutive year EPW topped customer satisfaction surveys, reporting the highest level since the survey began in 1997. EPW also owns an Energy Solutions business that advises customers on how to use less electricity, another unique and differentiating feature of their business. Although the Energy Solutions division is currently loss making having only been launched last year, we think the division could generate meaningful profits over the medium term; in light of the much-publicised record energy prices, there is a significant push by businesses to reduce energy costs

In 2015, EPW acquired a small US business called Source Power & Gas, in a move to replicate the business that they have refined here in Australia. In the short time since the acquisition, EPW have managed to secure 3rd place in terms of customer satisfaction out of over 50 retailers and have tripled the broker recognition rate, the key party in establishing new relationships. The US business is now close to break-even and we can see from the order book that rapid growth is set to continue. With a much larger addressable market, we believe the US based operation may eventually grow to become more profitable than the Australian one, more than doubling their retailing profits.

Lastly, the company has two Peaker power stations ("Peakers") called Oakey and Neerabup, which is the main reason why the company captured our attention initially. A Peaker is a quick start-up gas or diesel operated power station that provides power to the grid when prices are high, usually on a very hot or cold days or during the evening when everyone is operating appliances and the demand for power spikes. With the introduction of renewables in conjunction with coal power stations being shut down, the grid is becoming more unstable: South Australia is a well-publicised example of the consequences of such shifts in energy supply. Renewables are unable to provide baseload generation as effectively as coal and only work when the sun is shining or the wind is blowing, which often isn't the case during the evening when demand peaks. Though batteries are being touted as the solution to this problem, even the largest batteries currently in the world are unable to provide grid stability. As an example, the recently installed battery by Elon Musk in South Australia is the largest ever of its kind, and is still only able to provide power to 20,000 homes for just over an hour at its full capacity[1]. We think the easiest solution to this issue is to install Peakers in conjunction with renewables and batteries; when renewables are unable to meet peak power requirements, the Peakers will step in and take over the excess until demand falls again. Many Governments including South Australia have started to use this strategy, and at the time of this report a 210 MW gas-fired generator is being built for $295 million in South Australia by AGL[2] and another 276 MW of diesel and gas generation is being supplied by the Government at a cost of $339m to provide further stability.[3]

Therefore, we think the Peakers, especially Oakey, are valuable and underappreciated. Oakey is a Queensland based 332 MW power station in almost brand-new condition with an estimated replacement cost over $400m; this by itself exceeds the entire market capitalisation of EPW! While the asset is currently under-earning, as the grid becomes more unstable with renewables the asset will become much more profitable. The other Peaker, Neerapub, is a 50% owned 330 MW power station with a very long-term offtake agreement with the WA government. Although Neerapub's earnings are depressed due to a large amount of debt (which is ringfenced to the asset), the future for this asset is also very bright.

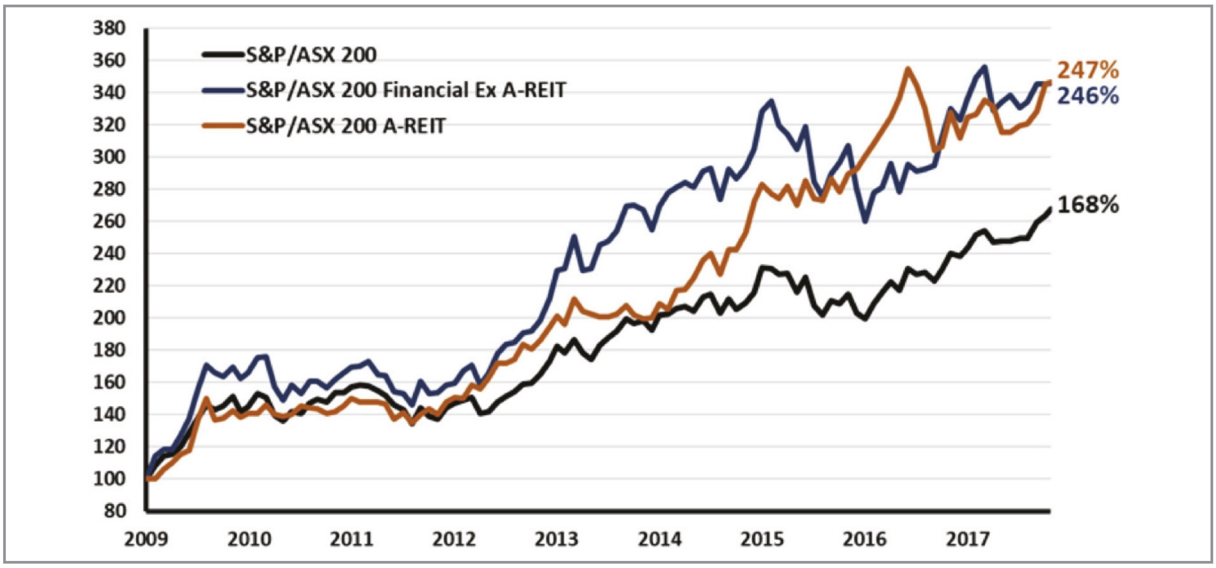
With a stable, profitable business in Australia, a growth driver in the US, and a replacement value asset backing that exceeds the entire value of the company, we think that ERM Power is an outstanding investment opportunity for our unit holders. Additionally, considering the nature of the business, we think it is relatively recession proof. Furthermore, while we wait for our investment thesis to play out over the next few years, we are collecting a ~5% fully franked dividend.

1. https://theconversation.com/explainer-what-can-teslas-giant-south-australian-battery-achieve-80738

2. http://www.abc.net.au/news/2017-06-07/agl-announces-new-sa-power-station/8596016

3. http://www.afr.com/business/banking-and-finance/diesel-generators-cost-339m-in-sa-power-fix-20171220-h08axd

LOOKING FORWARD

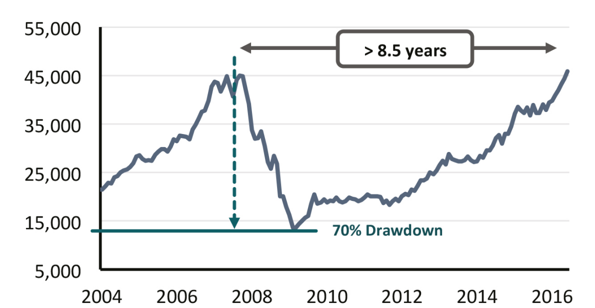


Source: FactSet

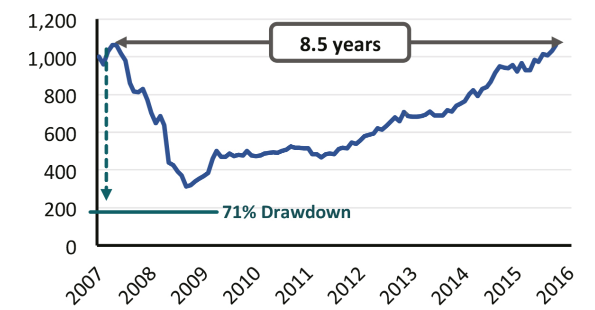
The sectors that have benefitted the most from the accommodating economic environment post the Global Financial Crisis of 2008/2009 have been Financials and REITs. These leveraged income generating asset classes have been in strong demand and currently represent approximately 43% of the S&P/ASX 200 Index.

Our intention is not to preach doom and gloom, and over the next few decades we are actually very optimistic regarding world growth and Australia in particular. However, using history as a guide, market excesses relating to leverage are from time to time painfully washed away and it can take several years for investors in these listed securities to recover their capital. From the trough of the Global Financial Crisis, it took the A-REIT and Financials ex A-REIT over 8 and 5 years respectively to recover investor capital on a total return basis.

S&P/ASX200 A-REIT Total Return[1]



Morningstar 5-Star Rated Property Fund[2]



Sources: 1. FactSet (XPJ-ASX) 2. Morningstar, Company Website

The new front line assets in our portfolio are either largely removed from the leverage cycle (GCS, ERM, ASB and TPI) or are in recovery, paying no dividend and currently only attractive to a small number of patient value investors such as ourselves. The year of 2017 was a necessary year of transition that we think sets up our investment performance for the next three years.

Please let me know if you have any questions and I look forward to catching up with you again soon.

Yours faithfully,

James Williamson
Fund Manager

APPENDIX

The Fund's Portfolio (unaudited)

As at 31 December 2017

Company Name	% of Fund
Captial Goods	12.1%
Software & Services	6.5%
Utilities	6.4%
Capital Goods	6.4%
Industrial Services	5.9%
Pharmaceuticals	5.8%
Commercial	5.0%
Energy	4.4%
Consumer Staples	4.1%
Financials	4.0%
Other Investments	18.9%
Total Equity Exposure	**79.5%**
Cash	20.5%
Total	**100%**

*Cash received on October 2nd following acceptance of a takeover offer.

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