WENTWORTH
WILLIAMSON

Quarter ending 31 March 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. 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. This 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 7.

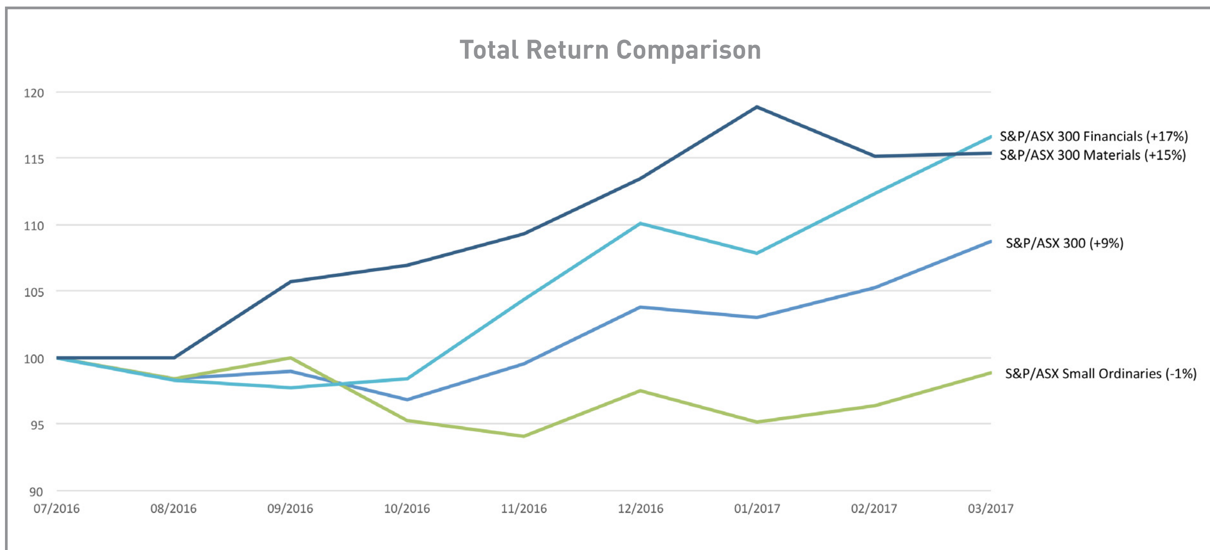
MARCH 2017 QUARTERLY REPORT

Returns (%)	WWF Fund	S&P/ASX 300 Accumulation Index	Relative Performance
Cumulative			
Since inception	45.7%	28.8%	**16.8%**
Annualised			
Since inception	11.3%	7.5%	**3.8%**
Latest 3 years	13.0%	7.5%	**5.5%**
Latest 2 years	12.9%	4.4%	**8.4%**
Latest 1 year	7.6%	20.2%	**-12.6%**

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.

In the first half of 2016 our Fund exited several companies after holding them for approximately three years, realising very pleasing returns. We think the recent weakness in some areas of the S&P ASX Small Ordinaries Index (see chart below), our 'sweet spot', has just given us the opportunity to re-position our Fund for another period of returns that you have been accustomed to since the inception of this trust. At the back end of the December quarter and early this year, our team initiated investments on four new companies for the Fund. This is a very high proportion of new investments in such a short period, considering we only normally activate on average two or three new positions a year. Furthermore, as you are aware, we typically only buy into companies that are currently out of favour with investors, meaning we often buy on the way down. There is far less buying competition and much more volume on the way down than the way up, so we are prepared to tolerate short term paper losses if it means we can secure a meaningful position in an exciting idea. Furthermore, if we have conviction there is significant upside from the first price we pay, our conviction should only increase when we buy it cheaper.

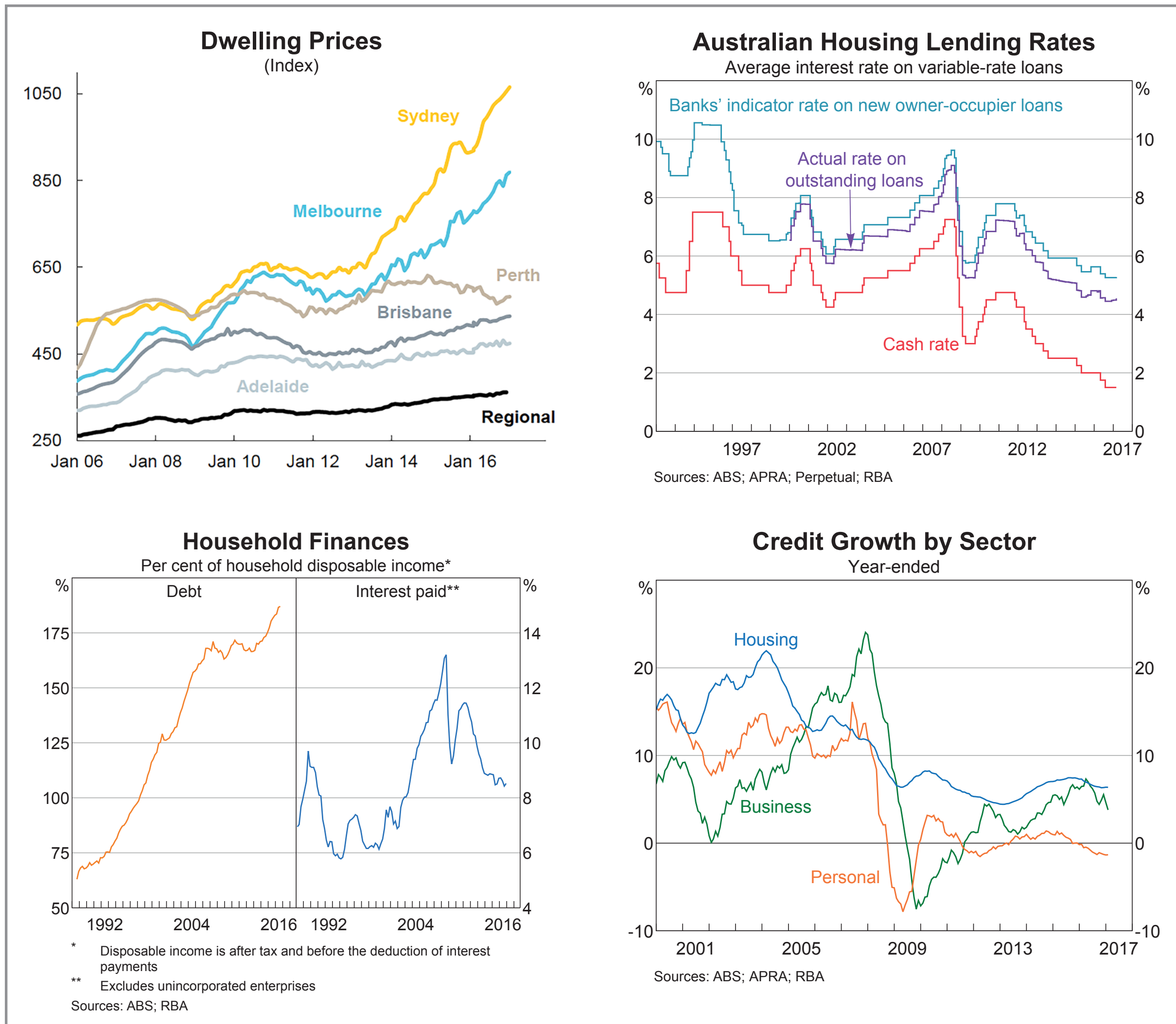
Considering we are bottom up, opportunistic stock pickers, we don't regularly spend time discussing the macro environment in our Quarterly Reports. However, this doesn't mean we don't keep abreast of the prevailing market climate, as well as which sectors have run and which have lagged. In the last few months, especially post the US election, the S&P/ASX 300 Accumulation Index has posted robust gains, but the performance has by no means been broad based across all sectors, as can be seen from the chart below.



Source: FactSet

If you cut down to it, the strong momentum rally has been propelled largely by companies with meaningful exposure to iron ore, as well as banks. Regarding iron ore, we are not comfortable making a long term call on Chinese demand for an abundant commodity with a flat cost/supply curve. While we acknowledge that we did not buy into this opportunity early last year, short term trading is not our game.

We also are not currently in the market to buy domestic banks. We do acknowledge that the stickier, largely deposit funded (liability) banks with large home loan exposure (assets) should over long periods of time be a better structure than some large banks offshore with higher wholesale funding (especially short term) and much lower home loan exposure. However, as the old saying goes 'the higher the price, the higher the risk'.



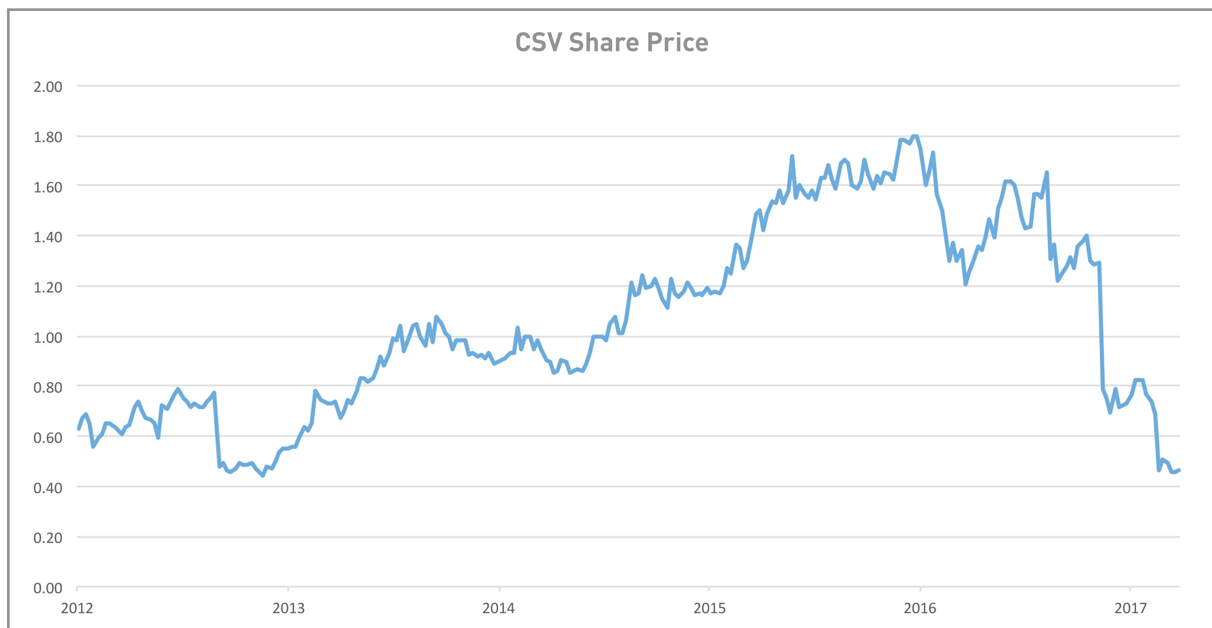
Source: CBA, RBA Website

We are truly travelling in unchartered territory. Lending rates are at all time low's, property prices continue to surge ahead at break neck speeds, and household debt to personal disposable income is not only at the highest level we have ever seen, but also amongst the highest in the world. Credit growth is no longer increasing at the mind boggling ~15-20% seen a decade and a half ago, but the current 7% growth still looks extraordinarily high to us given this backdrop.

In recent years, Australian banks have ramped up deposits as part of their funding mix and increased domestic home loan exposure, and are therefore more geared to the domestic economy today than they have ever been. The crux of this is that house prices, particularly in Sydney and Melbourne, look over valued on every metric. If for one reason or another the virtuous cycle of more debt → higher prices → more debt etc. gets disrupted by, for example, an international surprise like slower growth in China, or higher interest rates (let's keep in mind that ~40% of all home loans of the major banks are interest only), the multiplier effect for the domestic banks could be extremely damaging. At Wentworth Williamson, we don't short sell and I would be very hesitant to pick the timing of this unravelling anyhow. However, we remain confident that domestic banks do not represent an opportunity for our Fund over the next few years at current share price levels.

On the flip side, a lower price more often than not lowers the risk of capital loss. With this in mind, the significant recent share price falls for some growth orientated former market darlings in the S&P ASX Small Ordinaries Index has attracted our interest, and in some cases after due diligence, our capital. CSG Limited (CSV) is one of the new investments in the Fund, and we will take this opportunity to elaborate further on our thesis.

CSG LIMITED (CSV)



Source: FactSet

Let's start off by saying that CSV is a company we have previously researched and bought, having exited in 2015 at a handsome profit at a point where we felt it had reached fair value. Having done all the work, we continued to monitor this excellent company.

As can be seen from the chart above, the share price has collapsed in recent times, offering investors a rare opportunity to gain exposure to this quality company at a price we consider far below fair value. Many retail investors and smaller growth orientated funds have exited the company register en masse, market commentators have followed the share price down with their valuations (as they normally do), and hedge funds have accumulated a significant short position at the time of writing this note – negativity prevails for now! This is the type of scenario we look for all the time at Wentworth Williamson, however this time we are dealing with a company, as explained earlier, that we know quite well.

The company listed in 2007 with a market capitalisation of $169m, which remarkably is a larger value than today. At that time, the company consisted of two divisions: an IT business in the Northern Territory that provided outsourced IT infrastructure support, and a Xerox print business Centre in Queensland. The IT business posted rapid growth developing a national presence before eventually being sold to the Japanese company NEC Australia for $227.5m in July 2012. Much of this capital was returned to shareholders.

The current Managing Director of CSV, Julie-Ann Kerin, played a major role in growing the business as head of the division. Post the NEC acquisition it was a no brainer that CSV would make best efforts to retain Julie-Ann to take over the struggling Xerox print-as-a-service division, which principally bought printers/photocopiers from manufacturers and then leased the machines to SME's with a bundled annuity revenue package based on usage. It is important to note that the restraint of trade on CSV re-entering the IT services industry expired a year ago, an industry which Julie-Ann understands extremely well.

Today, CSV is in the process of completely disrupting the supply of goods and services from multiple vendors to SME's by bundling the offer of all products and services on one invoice; for a small business, having your print, IT and communications hardware and software, along with the accompanying maintenance and support, provided by one company for one fee saves a great deal of time and hassle. In doing so, CSV lock in clients for up to 5 years and charge a monthly subscription service fee per seat. The bundled offering can result in better quality products (as CSV has relationships with all the market leading product and service providers), superior service and convenience, all at a lower cost for the majority of SME clients. The initiative has been running for just over a year but the results and growth rates are incredible, as CSV has a first mover advantage and as far as we know, nobody else is doing

anything similar in Australia. It helps that CSV has a ~200,000 seat client base in their legacy print business that is essentially untapped and ripe for cross selling. By June 2017, the company is expected to have penetrated only ~10% of this client base with their new offering. Additionally, CSV recently signed an agreement with Officeworks to remarket their technology as a subscription bundle to their existing customers. Not only does the Officeworks agreement validate CSV's strategy, it opens an additional substantial captured client base. There is plenty of upside going forward and the overall market opportunity is enormous.

We are strongly of the view that the recent share price collapse is a complete overreaction to the company not hitting short term earnings guidance twice in a row. Short term sales for traditional legacy print equipment and hardware have been weaker than expected (in fact we think some of the transactions are only delayed and may well fall into the next fiscal year). At the same time, the EBITDA decline has been exaggerated because the company continues to invest and build its high-quality annuity technology with a service offering by recycling and strengthening its sales staff. This time around CSV is much more than a margin recovery story. The business has developed a unique customer offering that is disrupting traditional sales channels. The client growth on the annuity model is nothing short of exceptional, with the added bonus of locking in customers for ~5 years, a very rare feat in the industry. The unique and disruptive full product and service offering will provide a significant tailwind for this business over the next few years and it appears it is being completely ignored by the general market. This business, we believe, will look very different in a few years and should be rated much higher than it ever has been in the past. We are of the opinion that the company is worth multiples of its current market value.

LOOKING FORWARD

We can't predict the short-term price movements of our assets day to day and can't promise we won't have other down months amidst the wider market noise, but we truly believe our fund is positioned to offer significant upside over the long term when the underlying businesses perform as we expect them to.

Yours faithfully,

James Williamson
Fund Manager

APPENDIX

The Fund's Portfolio (unaudited)

As at 31 March 2017

Company Name	% of Fund
Software Services	7.0%
Capital Goods	6.6%
Commercial Services	6.3%
Commercial Services	6.2%
Industrial Services	5.9%
Utilities	5.9%
Software Services	4.4%
Capital Goods	4.2%
Oil & Gas	4.2%
Energy	4.0%
Other Investments	23.4%
Total Equity Exposure	**78.1%**
Cash	21.9%
Total	**100%**

COMPANY NAMES ONLY AVAILABLE TO UNIT HOLDERS

CONTACTS

Issued by Wentworth Williamson Management Pty Ltd
AFS Representative No. 445865
ACN 164 774 814

Level 18, 167 Macquarie Street, Sydney NSW 2000

Tel: +61 2 8052 5806
Email: james@wentworthwilliamson.com.au