MHOR AUSTRALIAN SMALL CAP

MONTHLY PERFORMANCE UPDATE

AS OF 31ST MARCH 2017

FUND RETURNED +1.57% (AFTER FEES)

NAV: 1.0313

PERFORMANCE TO BENCHMARK

	1 MONTH	3 MONTHS	SINCE INCEPTION
FUND	+1.57%	-6.09%	-3.66%
BENCHMARK	+2.66%	+1.46%	-1.09%
VALUE ADD	-1.10%	-7.55%	-2.58%

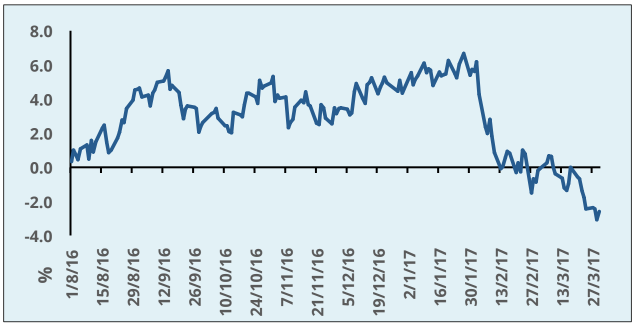
HISTORICAL PERFORMANCE

2017	JANUARY	FEBRUARY	MARCH
RETURN (%)	-2.03%	-5.62%	+1.57%

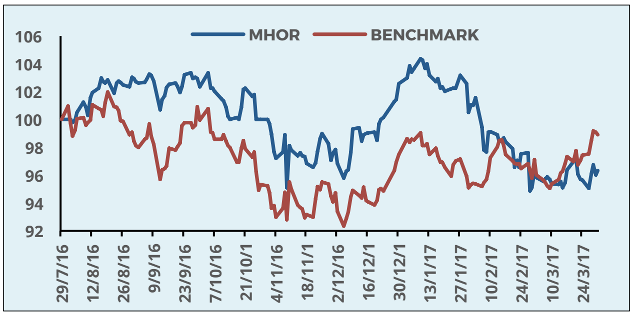
MHOR TOP CONTRIBUTORS – MARCH 2017

1	SPIRIT TELECOM	ST1
2	NEXTDC	NXT
3	AIRXPANDERS	AXP

CUMULATIVE PERFORMANCE OVER BENCHMARK



ABSOLUTE PERFORMANCE



OVERVIEW AND WELCOME

Welcome to the MHOR Small Cap Fund report for March 2017. The Fund returned +1.57% for the month, underperforming the benchmark index which was up 2.66%.

The MHOR Team was very busy during the month of March, meeting numerous management teams on their post-results roadshows, assessing many secondary capital raisings and IPOs and prosecuting our pipeline of investment ideas. The Small Cap market remains challenging with continued selling pressure evident, particularly at the less liquid end of the universe which we attribute to general risk aversion and in some cases Institutional mandates being moved from Small Caps, which can challenge the liquidity framework of the Small Cap market. Despite material share price moves the fundamentals of many Small Cap stocks remain unchanged in our view and we retain a broadly constructive outlook for Small Caps considering, in some cases, the sharp valuation correction and the relative growth on offer.

We think the growth outlook for many Small Caps compares favourably to Large Caps which have now rerated on the back of the reflation trade, much of this growth is driven by macro factors, including commodity prices which appear to be softening and it also appears that banks will be forced to slow their growth and post more regulatory capital to buffer against concerns around an overheated property market. If our thesis plays out, we anticipate Small Caps to once regain their outperformance over Large Caps based on superior growth offered at comparably cheaper prices.

We entered March with 30 stocks and 5.1% cash. Fund inflows remain modestly positive. We exited March with 31 stocks and 1.9% cash.

JAMES SPENCELEY

GARY ROLLO

+61 2 9191 9500 info@mhor.com.au www.mhor.com.au **ABN** 32 611 709 927

ABOUT THE MONTH

The Small Ordinaries index gained another 2.66% over the course of March, having risen 1.31% in February. Although the index has now printed two consecutive positive months, we note that volatility amongst sectors remains elevated with resources down c.4% in March on the back of softer commodity prices while industrials' outperformance during the month had much to do with several surprise corporate raids (Downer bidding for Spotless, Solomon Lew acquiring 10% of Myer and Ariadne snapping up 5% of Ardent) which drove short covering in a number of unloved names. Within the industrials space, discretionary retailers continue to underperform due to generally soft same store sales growth figures and fears about the impact of Amazon's entry into the domestic marketplace (we remain underweight discretionary retailers). The strong local housing sector is also attracting much attention (bubble fears) with the Australian Prudential Regulation Authority (APRA) stepping in with restrictions on interest-only loans in a bid to cool the market. With 'confession season' officially over, the number of profit warnings substantially decreased in March, the only notable offender being Fletcher Building (which we did not own). The market for secondary capital raisings and IPOs opened up again in March, having been temporarily closed for results season in February. As tends to be the case, we looked at many opportunities but chose to participate in only a select few. Further, we continue to observe selling pressure in the less liquid Small Cap universe as investors take a more defensive stance and likely compounded by capital flows out of Small Caps into other areas of the market as we observed in last month's report.

ABOUT THE PORTFOLIO

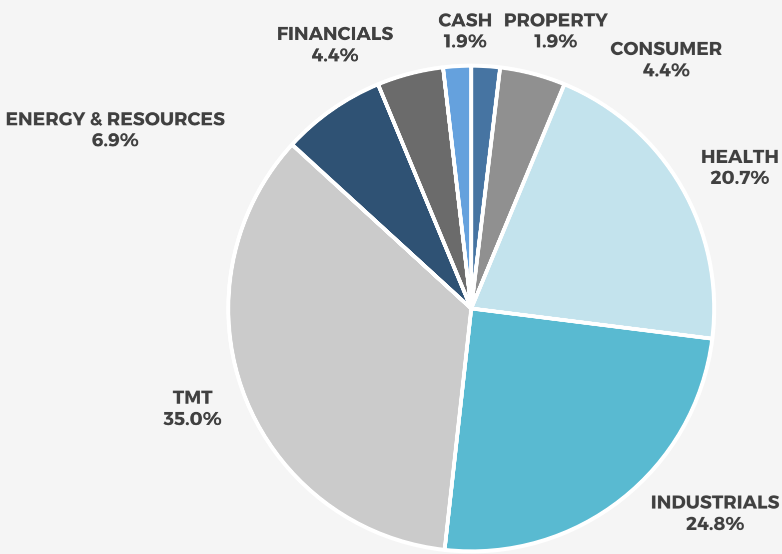
The Fund's largest positive contributions came from Spirit Telecom (ST1), NextDC (NXT) and AirXpanders (AXP). The major detractor for the month was Ellex Medical Lasers (ELX). More on each of these in the 'What happened in the Portfolio' section. The portfolio continues to have growth bias, has considerable exposure to smaller "undiscovered", we believe, attractive undervalued growth stories. We continue to search and find interesting new emerging small cap equity stories with little or no institutional ownership, picking those that have the scope to be discovered by larger small cap funds has so far served the fund well.

PORTFOLIO EXPOSURE AND METRICS

CHARACTERISTIC	PORTFOLIO	MARKET***
1YR FORWARD PE	14.3X*	14.9X
1YR FORWARD DIV. YIELD	3.1%	3.2%
2YR EPS GROWTH CAGR**	C. 20%	5.1%

*Ex Select early stage companies, ** MHOR and FactSet Consensus data, *** FactSet Consensus for Small Ordinaries Forward P/E

PORTFOLIO SECTOR EXPOSURES



+61 2 9191 9500 info@mhor.com.au www.mhor.com.au **ABN** 32 611 709 927

WHAT HAPPENED IN THE PORTFOLIO

Spirit Telecom (ST1) +23%. Our investment in Spirit Telecom generated solid gains for the portfolio during March. ST1 is a small but fast-growing ISP focused on supplying broadband services on next generation wireless infrastructure to multi-dwelling user locations including residential, business, student accommodation, community housing and business parks. Having followed the story for some time, and leveraging our industry expertise, we decided to invest in ST1 back in December 2016, participating in the capital raising which part funded the acquisition of Phone Names (13/1300/1800 smart numbers). In addition to the Phone Names deal being incredibly EPS accretive, we were attracted to the multi-year roll-out story emerging from the core business. With a market cap of just $30m, we continue to see significant upside potential for ST1, both organically and through further M&A.

NextDC (NXT) +10%. Backing up on its strong share price performance over February, NextDC once again made a positive contribution towards Fund performance in March. Pleasingly, the market appears to be gaining greater appreciation for NXT's structural drivers and attractive investment fundamentals. As Australia's only pure play data center operator, NXT provides strong leverage to the structural shift of enterprise resources to the cloud. We continue to maintain that market concerns over increasing competition have been overplayed with domestic demand for data storage expected to outpace industry supply for the foreseeable future. The majority of the base portfolio is contracted, generating solid cashflows, while strong market demand should ensure a relatively quick ramp up across the development assets (M2, S2 & B2), de-risking the story even further. Looking further out, NXT has the potential to double its current earnings base to meet anticipated domestic demand for data storage.

AirXpanders (AXP) +15%. Another key positive contributor to the Fund's performance in March was AirXpanders, a medical device company focused on commercializing its AeroForm Tissue Expander System used in breast reconstructions following mastectomy. We were pleased to see the stock rally having been sold off aggressively in February. We found the February share price weakness perplexing considering the company had only just raised A$45m of equity to fund the near-term growth strategy (build inventory, accelerate US sales and marketing, and complete the Costa Rica manufacturing plant) via a heavily oversubscribed equity placement. Nonetheless, we continue to regard AXP as a compelling investment proposition. The equity story has substantially de-risked after gaining US FDA *de novo* clearance in December and raising fresh equity in February to fund the substantial growth opportunity ahead. AXP has developed an innovative product which offers a superior solution to alternative procedures.

Ellex Medical Lasers (ELX) -14%. The major detractor to March's performance was Ellex Medical Lasers which designs, manufactures and sells medical devices to surgeons for the treatment of eye disease. There was little stock specific reason for the share price weakness of late, rather we suspect the market has been generally de-risking by selling less liquid, longer-dated growth stories such as ELX. Notwithstanding the more trepid market pulse, we remain attracted to ELX for a number of reasons. Firstly, and somewhat unusual for a medical device company, ELX has generated consistently solid growth in sales and profits from its core ophthalmic laser and ultrasound business (c.90% of Group sales), a business it has been involved in for over 30 years (market leading brand, c.40% market share, strong global relationships). Secondly, the company has significant growth potential from expanding into the fast-growing market for minimally invasive glaucoma surgery with its iTrack product (superior patient outcome, high reimbursement rate, large market). Thirdly, ELX also plans to grow in the emerging market for treating early stage age related macular degeneration with its 2RT product (Phase III data due late 2018, large addressable market, no alternative treatments available). Importantly, both of these new markets are each larger than ELX's core market. Finally, valuation is attractive – the $130m market cap does not appear to appropriately reflect the size of the opportunity.

OUTLOOK

Global equity markets remain buoyant, hovering around near all-time highs, spurred on by Trump's promised tax cuts, infrastructure investment, banking deregulation, as well as rising interest rates driving capital out of bonds. However, geopolitical risks have not abated; Trump is unpredictable and it remains unclear how the world will react to his protectionist agenda, Brexit is coming while Europe's upcoming elections will test the resolve of the Union, and China appears to have convinced the market it can manage an orderly slow down (for now). Domestically, we view the recent sell off in Small Caps as overdone – Large Cap valuations have increased yet commodity prices are softening while banks will likely be required to slow loan growth and increase regulatory capital. Meanwhile, the Small Cap market, which has experienced a material valuation correction, continues to present growth opportunities less correlated to broader macro forces.

HOW TO APPLY: APPLY ONLINE **HERE** OR DOWNLOAD THE APPLICATION FORM **HERE**

+61 2 9191 9500 info@mhor.com.au www.mhor.com.au **ABN** 32 611 709 927