August 2018

THE MONTGOMERY FUND

INVESTMENT REPORT & FACT SHEET

FUND OVERVIEW

The Montgomery Fund employs a bottom-up, value style to invest and manage the equity portfolio. The Fund has the ability to retain a cash weighting, with a 'soft' 30 per cent limit, while seeking to identify companies that satisfy three main points of criteria. For inclusion in The Montgomery Fund, a business must be of premium quality, display bright prospects for earnings and growth in intrinsic value, and be available to purchase at a reasonable price.

Pursuant to this objective, The Fund aims to deliver superior positive returns where suitable investment opportunities are abundant, and to preserve capital through cash allocations where suitable investment opportunities are scarce.

FUND FACTS

INVESTMENT MANAGER
Montgomery Investment Management Pty Ltd

OBJECTIVE
The Montgomery Fund aims to outperform the index over a rolling 5-year period.

BENCHMARK
The S&P/ASX 300 Accumulation Index

FUND CONSTRUCTION
The Fund's All Cap portfolio will typically comprise 20-40 high-conviction stocks listed on the ASX and/or NZSX. Cash typically ranges from 0%-30%, but up to 50% in extreme situations.

APIR
FHT0030AU

RECOMMENDED INVESTMENT TIMEFRAME
5 years

MINIMUM INITIAL INVESTMENT
$25,000

INCEPTION DATE
17 AUGUST 2012

FUND SIZE
$628.5M

MANAGEMENT FEE
1.36% per annum, which includes a management fee of 1.18% per annum. Both figures are GST inclusive and net of RITC.

PERFORMANCE FEES
15.38% of the total return of The Fund that is in excess of the Index. No performance fee is payable until any previous periods of underperformance has been made up.

APPLICATION & REDEMPTION PRICES
montinvest.com/tmf

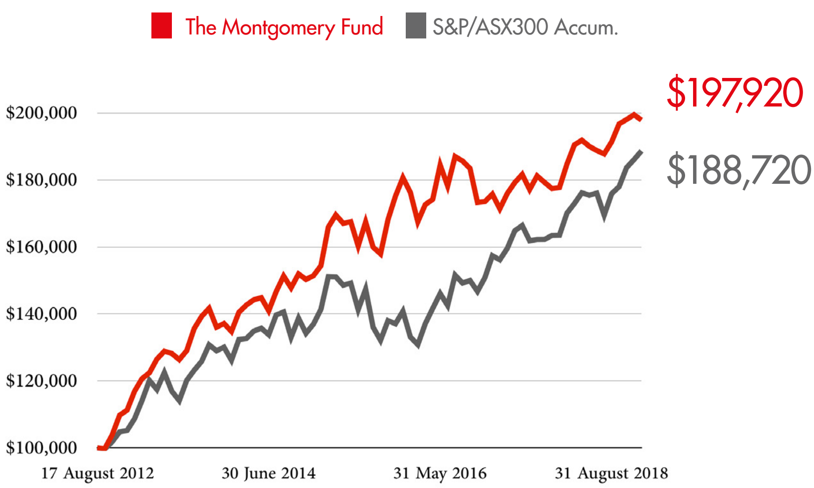
FINANCIAL YEAR RETURNS

FINANCIAL YEAR	THE MONTGOMERY FUND	S&P/ASX 300 ACCUM. INDEX
2013*	26.3%	14.1%
2014	11.6%	17.3%
2015	13.7%	5.6%
2016	11.2%	0.9%
2017	1.7%	13.8%
2018	9.3%	13.2%
Since Inception**	12.0%	11.1%*

* 2013 is the period 17 August 2012 to 30 June 2013

**Compound annual returns

PERFORMANCE GRAPH



PORTFOLIO PERFORMANCE

(to 31 August 2018, after all fees)

	INCOME	CAPITAL GROWTH	THE MONTGOMERY FUND	S&P/ASX 300 ACCUM. INDEX	OUT/UNDER PERFORMANCE
1 month	0.00%	-0.80%	-0.80%	1.40%	-2.20%
3 months	7.45%	-6.86%	0.59%	6.00%	-5.41%
6 months	7.76%	-2.96%	4.80%	7.17%	-2.37%
12 months	9.33%	2.19%	11.52%	15.45%	-3.93%
3 years (p.a.)	5.39%	1.97%	7.36%	11.53%	-4.17%
5 years (p.a.)	5.57%	2.28%	7.85%	8.91%	-1.06%
Since inception#	47.09%	50.83%	97.92%	88.72%	9.20%
Compound annual return (since inception)#	6.60%	5.37%	11.97%	11.09%	0.88%

\# *17 August 2012*

FUND COMMENTARY

The Australian equity market enjoyed a continuing positive mood through the August 2018 reporting season, rising by 1.4 per cent. As with any reporting season, there were some large price movements in both directions, but the overall tone of the market remained positive, with share price momentum continuing as a lead actor, particularly in some parts of the market, and valuation retaining more of a supporting role, at best.

The Montgomery Fund (The Fund) underperformed the broader market, declining in value by 0.8 per cent. While we were generally happy with the results reported by portfolio companies, two of The Fund's holdings – Primary Health Care and Speedcast International - delivered results announcements that disappointed the market, pulling an otherwise positive month into negative territory.

The most significant of these was Speedcast, a provider of satellite communications services, which delivered a result that fell short of expectations, and complicated the picture by simultaneously announcing a significant acquisition. The market's response was brutal, taking almost 40 per cent off the Speedcast share price in a single day.

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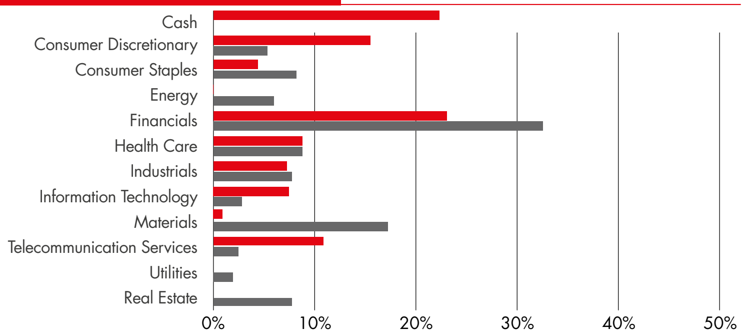
TOP COMPLETED HOLDINGS* (TCH)

(at 31 August 2018, out of 27 holdings)

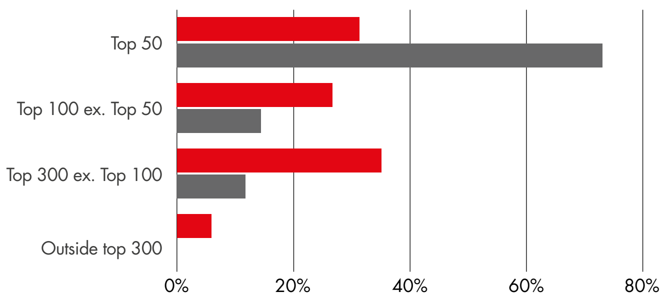
COMPANY NAME	RETURN ON EQUITY (%)	NET DEBT/EQUITY (%)	PRICE/EARNINGS (X)	WEIGHT (%)
Aristocrat Leisure	38.7	48.5	25.1	5.21
Spark New Zealand	24.0	69.6	16.5	4.76
Primary Health Care	3.7	42.6	16.7	4.46
Pendal Group	23.5	-24.3	14.6	4.11
Trade Me Group	13.1	8.5	20.1	3.90
Steadfast Group	8.0	-15.9	21.1	3.75
Westpac Banking Corp	13.4	N/A	12.2	3.74
National Australia Bank	12.8	N/A	12.2	3.67
Link Administration Holdings	14.3	29.3	16.7	3.44
Challenger	10.1	N/A	15.7	3.42
TCH AVERAGE	16.2	22.6	17.1	
MARKET AVERAGE	17.5	62.5	21.4	
Total equity weighting				77.9
Total cash weighting				22.1

Top Completed Holdings are businesses we own but are not actively buying or selling at the time of writing.

INDUSTRY EXPOSURE



MARKET CAPITALISATION EXPOSURE



TMF S&P/ASX300

PLATFORMS WE ARE ON: Ausmaq AMP PortfolioCare AMP Summit AMP Wealthview AMP North Asgard BT Wrap BT Panorama Colonial First Wrap Clearview Wealthsolutions Investment Exchange (IX) Federation Accounts HUB24 Linear Managed Accounts Macquarie Wrap MLC Wrap Navigator Netwealth IPDS Netwealth Super OneVue Powerwrap UBS

Over the subsequent days a team of three Montgomery analysts participated in the Speedcast conference call, attended a company briefing session, and met one-on-one with management. Following these sessions, all three of us arrived at the same conclusion, being that the initial communication of Speedcast's results was not well handled, and that the market reaction was unduly harsh relative to the underlying story and long-term potential value. In simple terms, the earnings shortfall relative to expectations was largely due to a much-anticipated ramp up in offshore oil drilling activity taking longer than expected to materialise (a timing issue), and the announced acquisition offered better valuation metrics than appeared at first glance.

Having reached this conclusion, and seeing limited further downside risk, we began adding to the position at prices of around $4.00 per share. While the Speedcast share price has subsequently recovered somewhat to around the mid $4.00s, and the late-August price may come to be seen as a rare buying opportunity, the impact to Fund performance for the month of August was significant.

In a similar vein, The Fund added to its position in Primary Health Care following its result, having come to the view that the market's response to the company's strategic growth initiatives and associated capital raising was unduly harsh, and viewing the 18 per cent price decline during August as a longer-term opportunity. Primary Health Care is undoubtedly undergoing a disruptive transformation under its recently-installed management team and earnings will be subdued in FY2019. However, having met with CEO, Dr Malcolm Parmenter, and his senior team on several occasions, we are confident in the turnaround plan being followed, and the capability of the team to execute that plan.

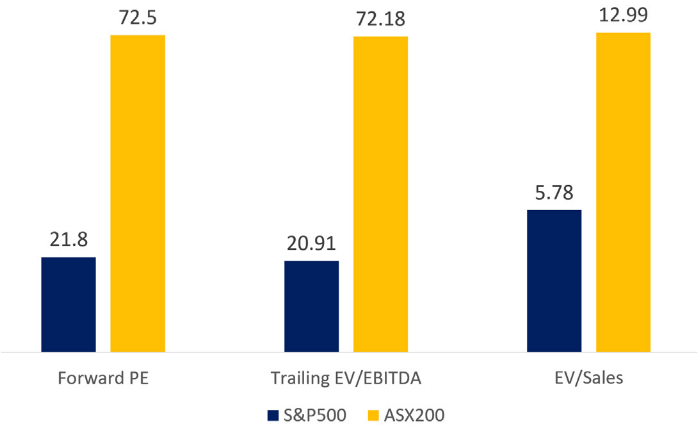
Looking more broadly at the market, as we have written in our recent updates, we are increasingly concerned at the level of optimism implicit in equity prices generally, and as the market advance has continued, we have moved The Fund to an increasingly conservative stance. This move involves holding significant levels of cash and moving away from stocks with higher growth rates and strong price momentum, towards those with a more secure and clearly-defined (typically lower growth) value proposition.

The valuation trends that have concerned us continued unabated during August, with the information technology sector of the S&P/ASX200 in particular continuing to rise rapidly, providing a useful case study of the multiples currently ascribed to high-growth companies.

The chart below sets out some aggregate valuation statistics for the 14 information technology companies in the ASX200 Index, alongside the same statistics for the 73 information technology companies in the US S&P500 Index.

As shown in the chart, ASX200 Information Technology companies currently trade in aggregate at strongly elevated multiples, both in absolute terms, and also in comparison with IT businesses in the US. While some of the ASX-listed IT companies will no doubt prove to be good investments long term, we think it is a striking comparison that the Australian IT sector trades at a forward PE multiple in the region of 70 times, while companies like Apple, Facebook and Alphabet trade at forward PE multiples in the region of 20 times.

Information Technology Sector Trading Multiples (x)



Source: Bloomberg

It is impossible to know when the market's eagerness to pay high multiples for high-growth companies may abate, but we believe that the current valuation environment provides a poor balance of downside and upside risk for investors in these types of companies. Accordingly, while we are attracted to them on quality grounds, we remain wary of owning them in the current market.

This stance will most likely to hold back relative performance for The Fund in the months ahead, but may provide very meaningful protection of capital over a longer horizon.