

K2 Australian Small Cap Fund (Hedge Fund)

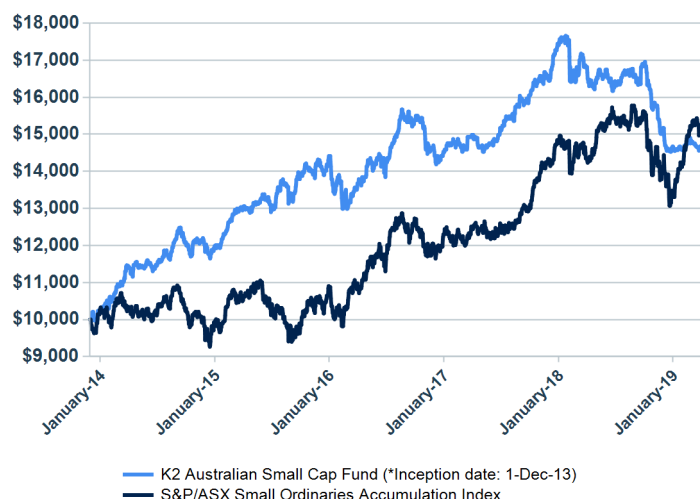
31 March 2019



The K2 Australian Small Cap Fund is an Absolute Return equities fund. The fund is index-unaware, aiming to produce positive absolute returns over the long term with a capital preservation mindset. The Funds' mandate allows it to actively manage its net market exposure – utilising both cash and shorts to help protect clients' capital.

	1 Month	3 Months	1 Year	3 Years (%pa)	5 Years (%pa)	Inception (%pa)	Inception Date
Performance (Net of Fees)	-1.1%	0.0%	-12.7%	2.4%	5.1%	7.5%	1-Dec-2013
Average Net Exposure	44.5%	37.7%	62.2%	75.5%	76.5%	75.5%	

Growth of \$10,000



Commentary

The K2 Australian Small Cap Fund returned -1.1% for the month of March.

Global markets ended the quarter on a high as investors continued to embrace risk assets. Global bond yields reached new depths, with the Australian 10YR yields contracting by 100bps over the last 4 months to a low of 1.72%, their lowest level since Federation. This repricing in the cost of capital has sent long duration assets soaring with infrastructure companies and REITs being a major beneficiary while investors have re-rated companies that exhibit long-term 'structural' growth. Overall, the ASX Small Ordinaries Accumulation Index decreased -0.1%. The Small Ordinaries, excluding resources, is now trading on a multiple of over 20x 2019 expected earnings, as technology and healthcare sectors are enjoying phenomenal valuations, with PE multiples approaching 50x and 30x respectively. Despite these lofty expectations, earnings expectations continue to decrease. Profit growth for 2019 is now anticipated to be 12%, down from over 20% just 3 months ago.

Collins Food (CKF) is a new addition to the Fund. CKF is a KFC franchisee across Australia and Europe and Taco Bell Australia. We are attracted to the defensive nature of the industry, while the store rollout across the Taco Bell network provides a strong runway for growth. The recent takeover of Restaurant Brands, CKF's closest peer, also highlights the strategic value of the business.

The Fund remains cautiously positioned, with 49% net exposure, up 10% from the previous month end. We are wary about the outlook for Australian equities. Domestic economic activity is slowing, corporate operating costs are tending to rise and bureaucratic interference is increasing. This was illustrated at the most recent reporting season, with the largest negative EPS revisions since the GFC. Given this weak earnings backdrop and after a decade of asset price appreciation, valuation metrics should gradually taper. Lower valuation multiples and fading profits do not normally equate to strong equity market gains.

Top 5 Stock Holdings	Current	Monthly Move
Elanor Investor Group	3.9%	+0.1%
Cedar Woods Properties Ltd	3.3%	+0.0%
Metlifecare Ltd	3.0%	+0.1%
Healthia Ltd	2.9%	+0.0%
Seven Group Holdings Ltd	2.6%	+1.4%

Month End Exposures	Current	Monthly Move
Communication Services	2.1%	+2.1%
Consumer	9.9%	+2.7%
Financials	11.5%	+1.1%
Health Care	7.9%	+0.3%
Industrials	6.0%	+1.6%
Information Technology	3.0%	+0.8%
Materials	5.5%	+0.9%
Real Estate	4.0%	+0.0%
Utilities	0.7%	-0.1%
SHORTS	-1.4%	+0.4%
Number of Positions	34	+3
Gross Equity Exposure	52.0%	+9.0%
Cash Weighting	50.7%	-9.9%
Net Equity Exposure	49.3%	+9.9%

Fund Characteristics

FUM	AUD \$24m
Portfolio Managers	Campbell Neal, David Poppenbeek, Josh Kitchen and Nicholas Leitl
Strategy	Australian and New Zealand Small Cap Equities
Objectives	To deliver consistent absolute returns over the investment cycle with a focus on capital protection during periods of market declines
Return Target	+10% pa over the long term
Number of Stocks	Up to 100
Cash	Up to 100% of portfolio
Distributions	Annually
Management Fee	1.31%
Buy/Sell	Bought and Sold on the ASX market (ASX: KSM)
Performance Fee	15.38% pa of the amount by which the NAV per unit exceeds the High Water Mark once the fund achieves its hurdle

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K2 Australian Small Cap Fund Net Monthly Returns in AUD

Year	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Fin YTD	Fin YTD Index (1)	Average Cash	Average Short
2013/14						2.9	3.2	3.1	4.4	0.4	1.2	-1.3	14.5	1.1	41.9%	0.0%
2014/15	3.6	2.6	-0.7	0.5	-1.0	-0.4	2.6	4.5	1.4	-0.2	2.2	-2.1	13.5	0.4	22.5%	0.0%
2015/16	5.7	-2.8	3.6	1.6	1.3	1.2	-4.0	-5.8	4.8	3.3	1.2	-0.4	9.6	14.4	12.5%	-0.2%
2016/17	4.8	3.1	0.0	-1.5	-3.8	-0.4	1.6	-1.5	3.1	-2.3	0.8	2.8	6.5	7.0	15.9%	-0.5%
2017/18	2.1	3.6	0.1	2.9	-0.2	5.9	-0.3	-3.4	0.0	-2.1	1.7	-1.9	8.3	24.2	21.3%	-2.0%
2018/19	1.8	-1.0	2.1	-6.3	-4.2	-3.3	-0.4	1.5	-1.1				-10.7	-1.8	45.2%	-4.3%
												Incept	46.7	51.8		
												Incept	7.5%pa	8.1%pa	26.6%	-1.2%

(1) S&P/ASX Small Ordinaries Accumulation Index

DISCLAIMER: Returns are shown after fees (including performance fees) and expenses have been deducted and assume the reinvestment of income distributions. Please note that past performance is not a reliable indicator of future performance. The information contained in this document is produced by K2 Asset Management Ltd ("K2") in good faith, but does not constitute any representation or offer by K2. It is subject to change without notice, and is intended as general information only and is not complete or definitive. K2 does not accept any responsibility, and disclaims any liability whatsoever for loss caused to any party by reliance on the information in this document. A product disclosure statement or information memorandum for general information on any Fund referred to in this document can be obtained at www.k2am.com.au or by contacting K2. You should read the product disclosure statement and consider whether the product is appropriate for you before making a decision to acquire or continue to hold an interest in a Fund. Fees referred to in this document are inclusive of GST and RITC and do not include expense recoveries.