



## KSM - K2 Australian Small Cap Fund (Hedge Fund) Monthly Report - 31 January 2017

### Australian Small Cap Market Review

The K2 Australian Small Cap Fund returned 1.57% for the month of January.

Global equity markets continued to be driven by political noise and positioning in January as the US president-elect became Mr President. Trump moved quickly to sign multiple executive actions, a clear message that he won't back down from pre-election promises. While appealing to some circles, his actions have disappointed many others and it's this social divide that requires ongoing thought. Although not as prevalent as prior months, the deflation theme continued as large cap value and cyclicals outperformed small caps. Multiple earnings updates did little to help sentiment, resulting in additional de-risking ahead of 1H17 results. International growth stocks ACX and SRV lowered expectations, while domestically focused companies also encountered problems with VRT, VRL and MEA downgrading. While each of these had their own intricacies, domestic demand does require close monitoring going forward.

### Portfolio Insight: Smart Parking (SPZ)

Smart Parking (SPZ) is a company we have been watching for some time, recently initiating a position in the November capital raising. SPZ provide global car parking solutions with a significant focus on the UK. The opportunity sits within the Management Services division (90% of group revenues) which uses Automatic Number Plate Recognition (ANPR) technology to provide ticketless and barrier free parking systems. As of October this technology was deployed in 190 sites with new installations running at ~10 per month. This rate likely accelerates now that the company is fully funded, a strategy we strongly endorse. Additional sites require minimal capex at ~£15,000, while generating monthly ANPR revenue of ~£6,000 at an EBITDA margin of 70%. With the Management Services division delivering an FY16 EBITDA margin of 18.9%, we expect significant operating leverage and earnings growth as new sites are added over coming periods.

The smaller Technology business remains loss making, but recent contract wins are encouraging. The R&D within this division should also result in technology which can be monetised through the broader Management Services division over time. We view December's contract to supply, install, and maintain a city wide deployment of over 3,000 parking bay sensors, ANPR technology and smartphone application to the City of Cardiff Council as a positive signpost.

Post capital raise we believe SPZ is fully funded and on the verge of explosive earnings growth. As a result, we see significant upside as more sites are added and awareness of the story improves throughout 2017.

### Outlook

In our view, equities remain the asset class of choice as bond yields normalise further in 2017. While the small cap space has experienced significant volatility in recent months, we continue to find companies with strong growth profiles trading at a sizeable discount to market. Strong commodity prices and a large harvest have turbo-charged the terms of trade in the short-term and the outlook for the domestic economy remains bright. We expect business investment to follow as a result. The downgrades of VRT, VRL and MEA are all of note, however, given their exposure to discretionary spending. While not a red flag on its own, we will closely monitor holiday trading updates in the retail sector for additional signposts on the health of consumer spending.

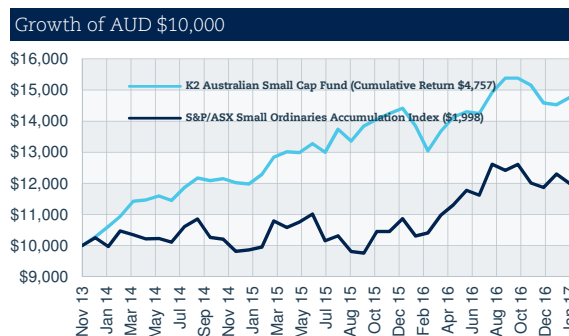
The median PE of our portfolio is 13.1x with earnings growth of 14%. This is clear evidence of the opportunities within the small cap space, and we continue to assess companies which possess a clear catalyst to re-rate. The Fund ended the month with 98% net equity exposure and we feel our portfolio is well positioned for what is sure to be an intriguing year under President Donald Trump.

### Top 5 Stock Contributions - January

<b>Largest</b>	Centuria Capital Group, IVE Group Ltd, Medical Developments International, Money3 Corp Ltd, Think Childcare Ltd
<b>Smallest</b>	Capilano Honey Ltd, Corporate Travel Management, Mantra Group Ltd, PWR Holdings Ltd, Yowie Group Ltd

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Performance to 31 January 2017 (net of fees)	
1 Month	1.57%
3 Months	-2.63%
6 Months	-1.15%
1 Year	6.58%
3 Years (pa)	11.61%
Since Inception (pa)	13.07%



Returns are based on NAV per unit plus distributions reinvested net of management fee and performance fee accruals. The method for calculating the NAV is set out in the Fund's PDS.

Fund Details (Unaudited)	
NAV Per Unit:	A\$2.59
Fund Size:	A\$20.9m
Start Date:	1-Dec-13

Top 5 Holdings	Sector	%
Medical Developments International	Cons. Non-Cyc	5.2
Think Childcare Ltd	Cons. Non-Cyc	4.0
Motorcycle Holdings Ltd	Cons. Cyclical	3.8
Baby Bunting Group Ltd	Cons. Cyclical	3.8
Peet Ltd	Financial	3.6

Sector Exposure %			
	Long	Short	Net Equity
Basic Materials	2.7	-	2.7
Communication	7.0	-	7.0
Cons. Cyclical	20.4	-	20.4
Cons. Non-Cyc	24.5	-	24.5
Energy	0.5	-	0.5
Financial	27.6	-	27.6
Industrial	5.8	-	5.8
Technology	9.2	-	9.2
<b>Total Equity</b>	<b>97.6</b>	<b>-</b>	<b>97.6</b>
<b>Total Cash</b>			<b>2.4</b>
<b>Total Equity and Cash Exposure</b>			<b>100.0</b>