



MONTGOMERY



Growing Income Trumps High Yield



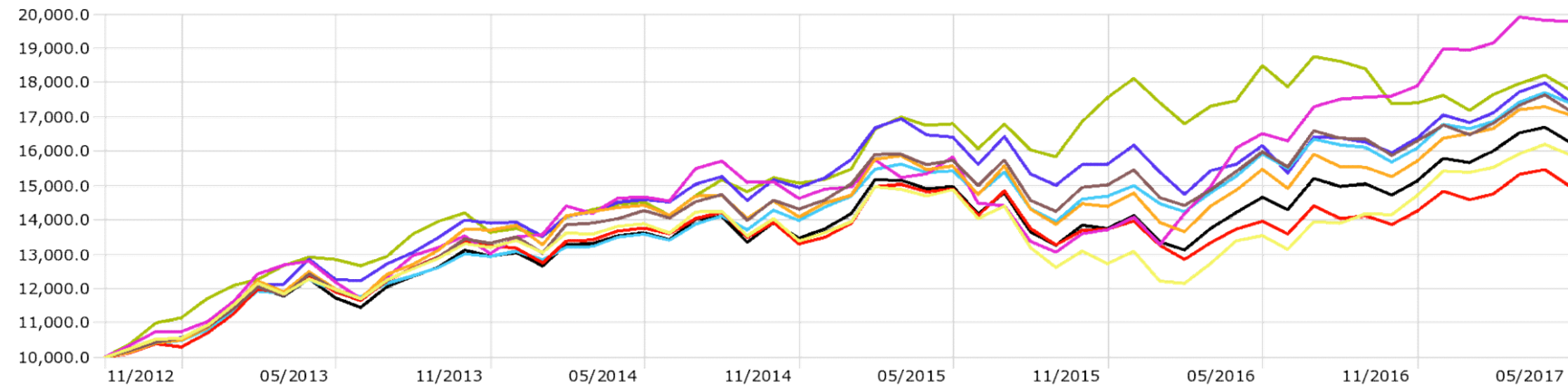
Roger Montgomery
Chief Investment Officer
August 2017

Manager Analysis



Growth of \$10,000

Time Period: 1/09/2012 to 31/05/2017



The Montgomery Fund	17,776.7	Schroder Australian Equity Fund	15,889.4	Fidelity Australian Equities	17,168.7
Ausbil Australian Active Equity	17,053.9	Allan Gray Australia Equity A	19,797.9	UBS Australian Share Fund	14,965.0
Investors Mutual WS Australian Share	17,399.6	Perpetual Wholesale Industrial	17,424.2	S&P/ASX 300 TR	16,249.2

Performance

Time Period: 1/09/2012 to 31/05/2017

	Return	Cumulative Return	Standard Deviation	Excess Return	Information Ratio (arith)	Sharpe Ratio (arith)	Tracking Error
The Montgomery Fund	12.88	77.77	10.73	2.11	0.29	0.52	7.41
Schroder Australian Equity Fund	10.24	58.89	11.87	-0.52	-0.16	0.24	3.16
Fidelity Australian Equities	12.05	71.69	11.39	1.29	0.57	0.41	2.26
Ausbil Australian Active Equity	11.89	70.54	12.42	1.13	0.45	0.37	2.52
Allan Gray Australia Equity A	15.46	97.98	12.70	4.70	0.60	0.64	7.87
UBS Australian Share Fund	8.86	49.65	11.70	-1.90	-0.78	0.13	2.43
Investors Mutual WS Australian Share	12.37	74.00	9.70	1.61	0.50	0.52	3.21
Perpetual Wholesale Industrial	12.40	74.24	11.47	1.64	0.47	0.44	3.52
S&P/ASX 300 TR	10.76	62.49	11.72	0.00		0.29	0.00

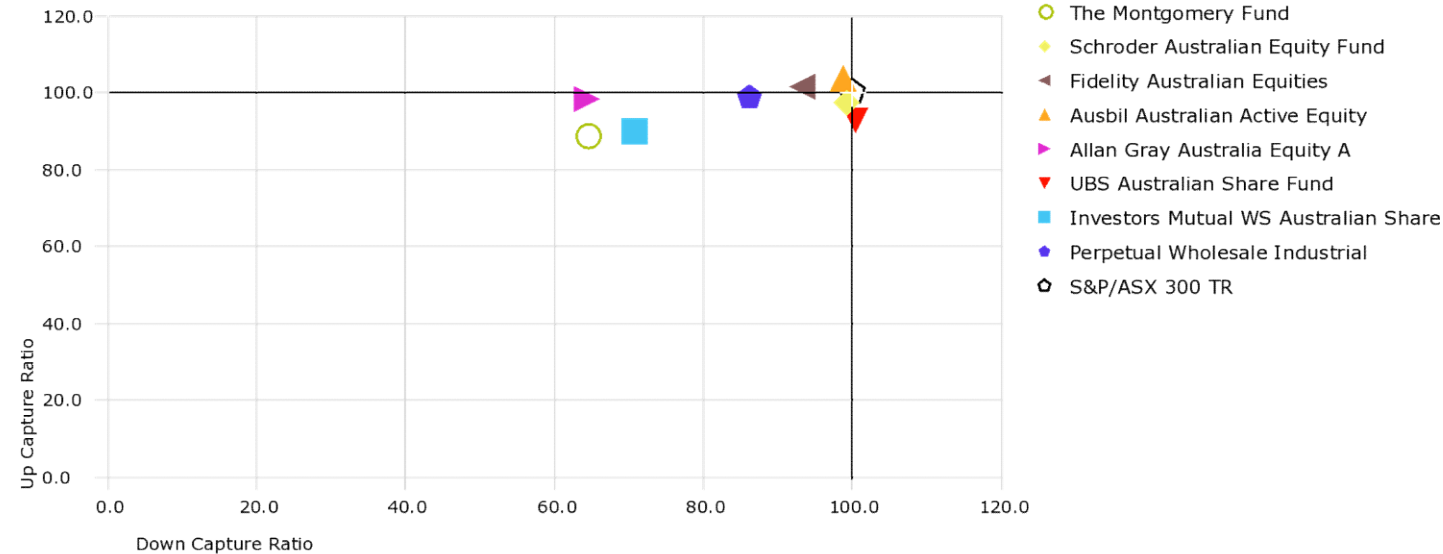
Manager Analysis



Upside-Downside Capture

Time Period: 1/09/2012 to 31/05/2017

Peer Group (5-95%): Open End Funds - Australia - Equity Australia Mid/Small Growth



Market Performance

Time Period: 1/09/2012 to 31/05/2017

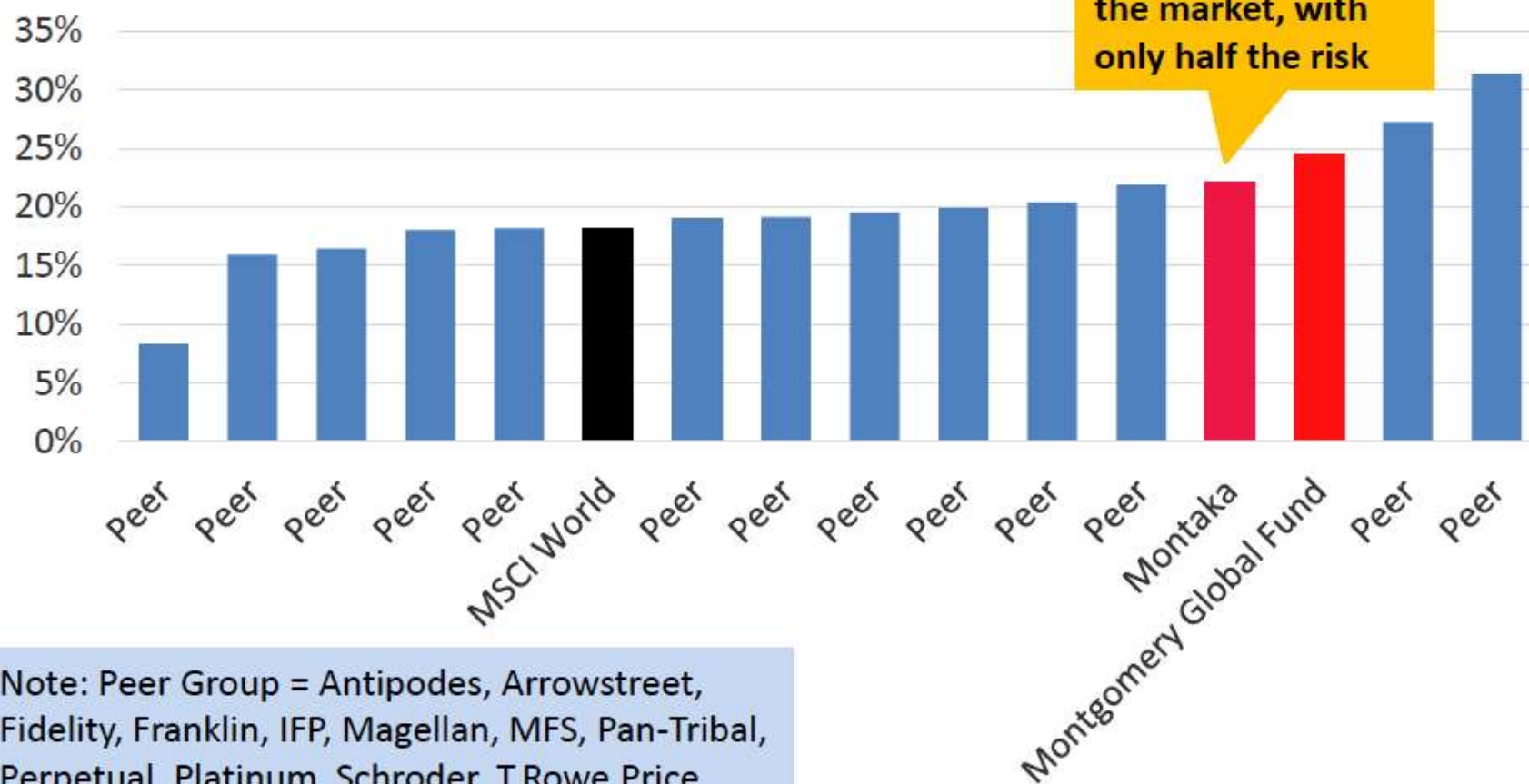
	Up Period Percent	Down Period Percent	Best Month	Worst Month	Best Quarter	Worst Quarter	Up Capture Ratio	Down Capture Ratio	R2
The Montgomery Fund	66.67	33.33	7.50	-5.53	14.41	-5.45	88.46	64.72	81.53
Schroder Australian Equity Fund	61.40	38.60	7.26	-8.41	10.03	-10.16	97.50	99.28	96.67
Fidelity Australian Equities	64.91	35.09	6.77	-7.48	10.35	-5.70	101.31	93.24	98.33
Ausbil Australian Active Equity	64.91	35.09	7.09	-8.09	12.01	-7.16	103.89	98.88	97.99
Allan Gray Australia Equity A	70.18	29.82	7.46	-8.54	14.90	-9.83	98.26	64.28	82.05
UBS Australian Share Fund	63.16	36.84	7.66	-7.38	11.41	-6.07	92.54	100.41	98.01
Investors Mutual WS Australian Share	64.91	35.09	5.49	-6.90	9.69	-5.60	89.82	70.71	97.91
Perpetual Wholesale Industrial	63.16	36.84	6.85	-6.66	11.66	-7.86	98.74	86.28	95.85
S&P/ASX 300 TR	63.16	36.84	6.92	-7.70	10.31	-6.48	100.00	100.00	100.00
25th Percentile	63.16	43.86	11.04	-6.62	18.30	-8.35	101.19	91.50	82.12
50th Percentile	57.89	42.11	9.64	-7.78	17.47	-9.14	85.50	79.67	80.01
75th Percentile	56.14	36.84	8.55	-8.23	14.66	-11.01	78.10	63.36	77.73

Source: Morningstar Direct

MONTAKA AND MGF — PEER GROUP ANALYSIS

Performance Comparison

Fund Performance, After Expenses (1 July 2015 to 31 May 2017)

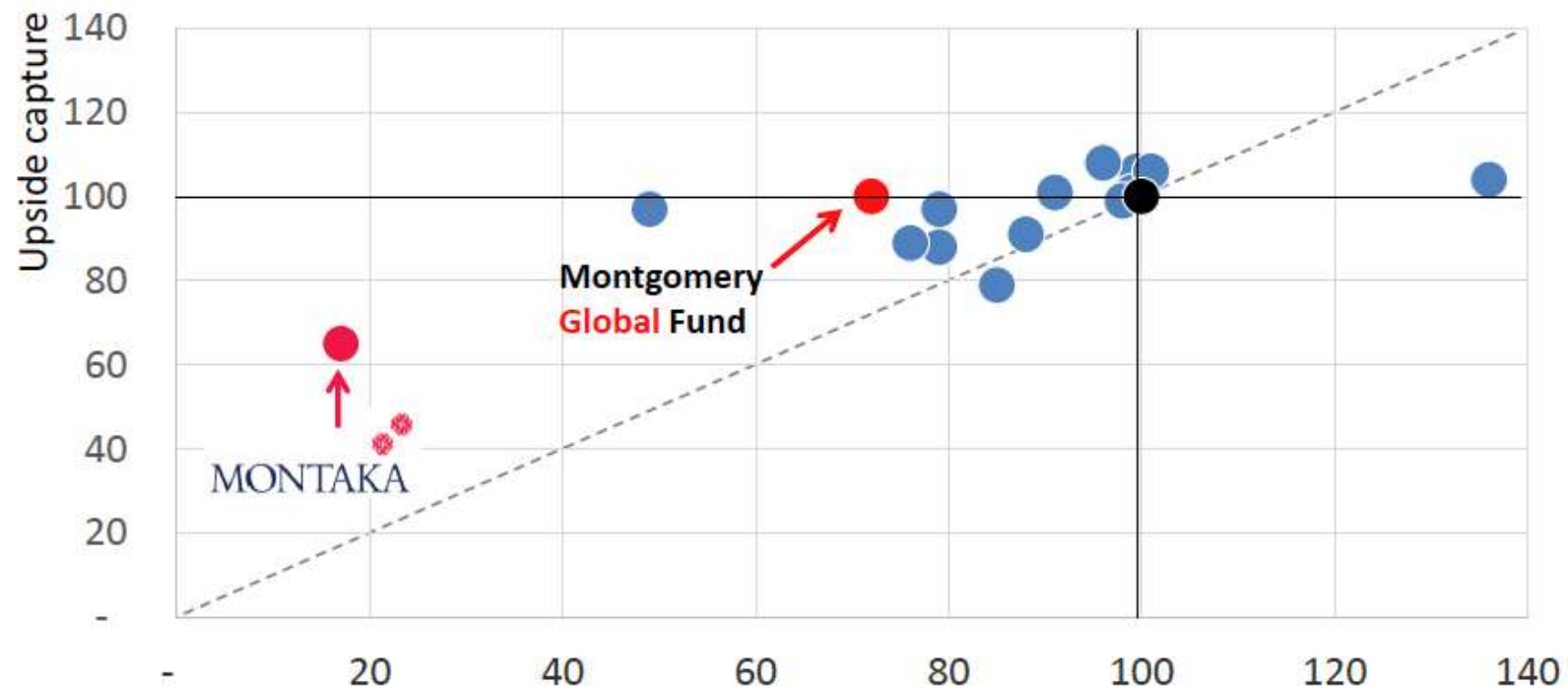


Note: Peer Group = Antipodes, Arrowstreet, Fidelity, Franklin, IFP, Magellan, MFS, Pan-Tribal, Perpetual, Platinum, Schroder, T.Rowe Price, Walter Scott

MONTAKA AND MGF — PEER GROUP ANALYSIS

Upside-Downside Capture

Fund Performance, After Expenses (1 July 2015 to 31 May 2017)

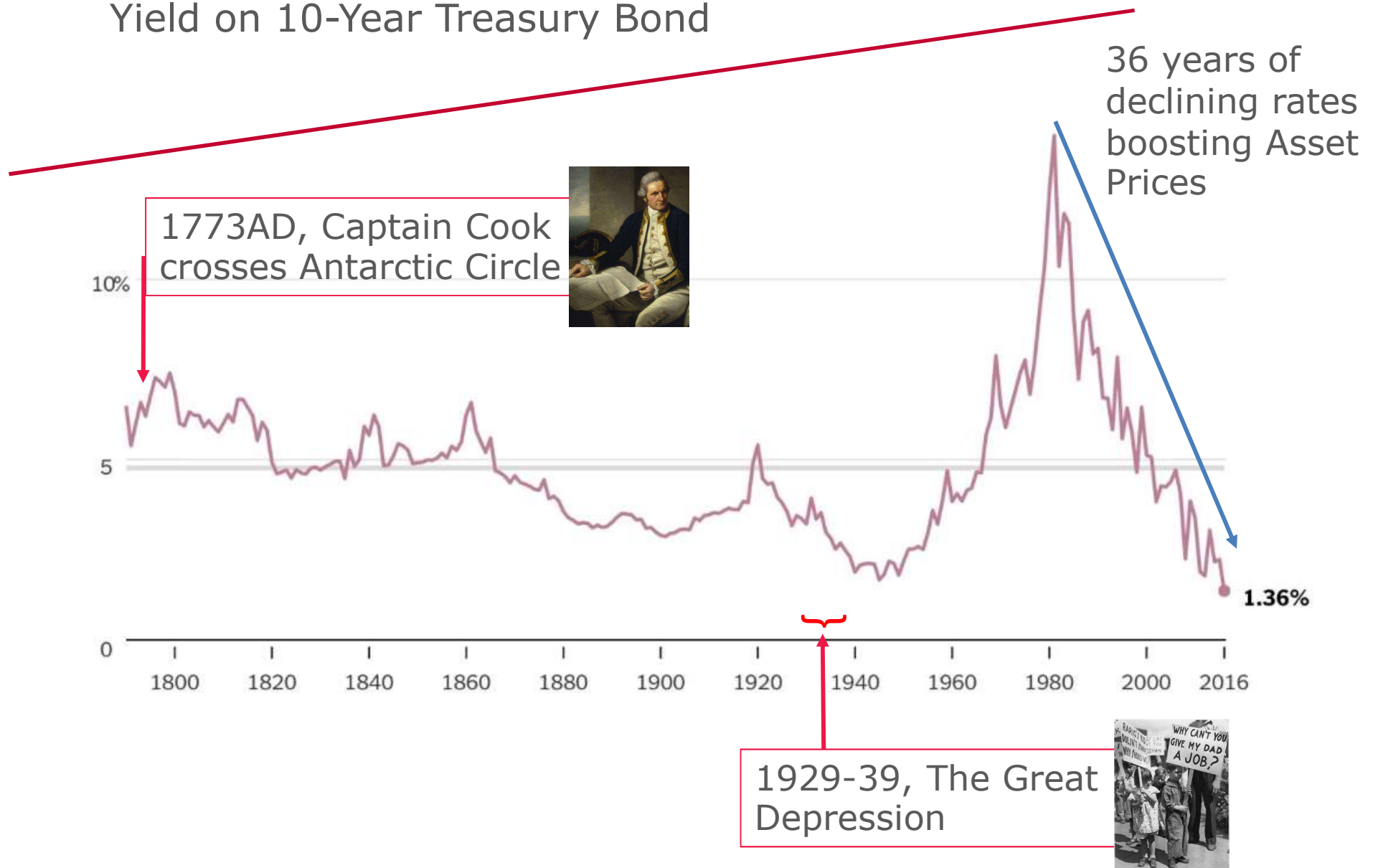


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Source: Morningstar; MGIM

Rates Lower than the Great Depression

Yield on 10-Year Treasury Bond



Australian rates at historic lows

Pressure on savers

17.5%



1.5% (91% decline)

“Cash is a liability” 2017

“cash is king” 1990



Nil income assets fetch the most

Basquiat



Nil income assets fetch the most USA



Peter Doig's *Rosedale* (1991) had an on-request presale estimate said to be \$25 million, and sold for \$28.8 million with premium.
COURTESY PHILLIPS / PHILLIPS.COM

Nil income assets fetch the most
NSW



Nil income assets fetch the most
NSW



**Nil income assets fetch the most
NSW**



Nil income assets fetch the most

Victoria



Nil income assets fetch the most
USA

**Hermes Handbag's Auction
Record: \$380K for Croc Skin
Purse**



PE Ratio at near record highs

S&P500 Shiller PE*



*Average inflation-adjusted earnings from the previous 10 years, a.k.a. Cyclically Adjusted PE Ratio (CAPE Ratio)

Australian Experience

Near prior extremes



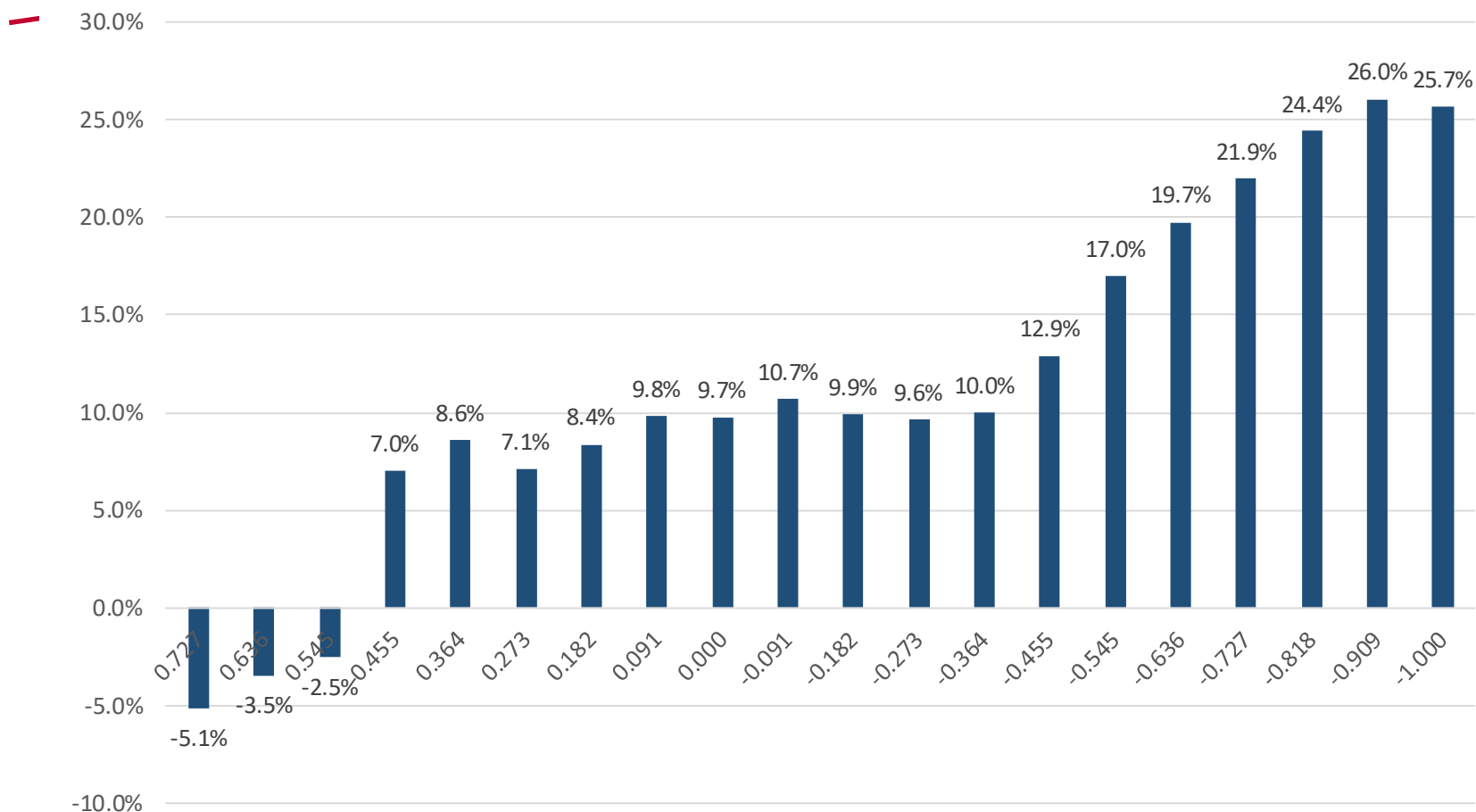
Average PE = 18x. (7% higher than October 2007)

Growth in forecast earnings = 19% of appreciation in 5yrs

PE Expansion = 81% of appreciation in 5yrs

Equal-Weighted Total Return by Quality

12 months to December 31, 2016



Growing Income versus Yield

How to put yourself in danger

	Year 1	Year 2	Year 3
Equity(b)	\$10.00	\$10.00	\$10.00
ROE	20%	20%	20%
EPS	\$2.00	\$2.00	\$2.00
POR	100%	100%	100%
DPS	\$2.00	\$2.00	\$2.00
Equity(e)	\$10.00	\$10.00	\$10.00
P/E	10	10	10
Share Price	\$20.00		\$20.00
Cash Flows	-\$20.00	\$2.00	\$22.00
IRR			10%

Yield =
10%

Growing Income versus Yield




How to put yourself in danger

One dollar in 1977 is worth just 16.74 cents in today.*

*Based on inflation statistics from ABS 1977-2017. High 12.20% 1977, low 1% 1992. Average 4.58%

Growing Income versus Yield

How to put yourself in danger

2005			
Investment	\$100,000	\$100,000	\$100,000
Price	\$0.32	\$4.69	\$9.09
Dividend	\$0.01	\$0.28	\$0.47 *
Yield	3.91%	5.97%	5.17%
Total Income	\$3,910	\$5,970	\$5,171
Return on Equity	18%-32%	26%-35%	24%-49%
Payout Ratio	75%	99%	39%

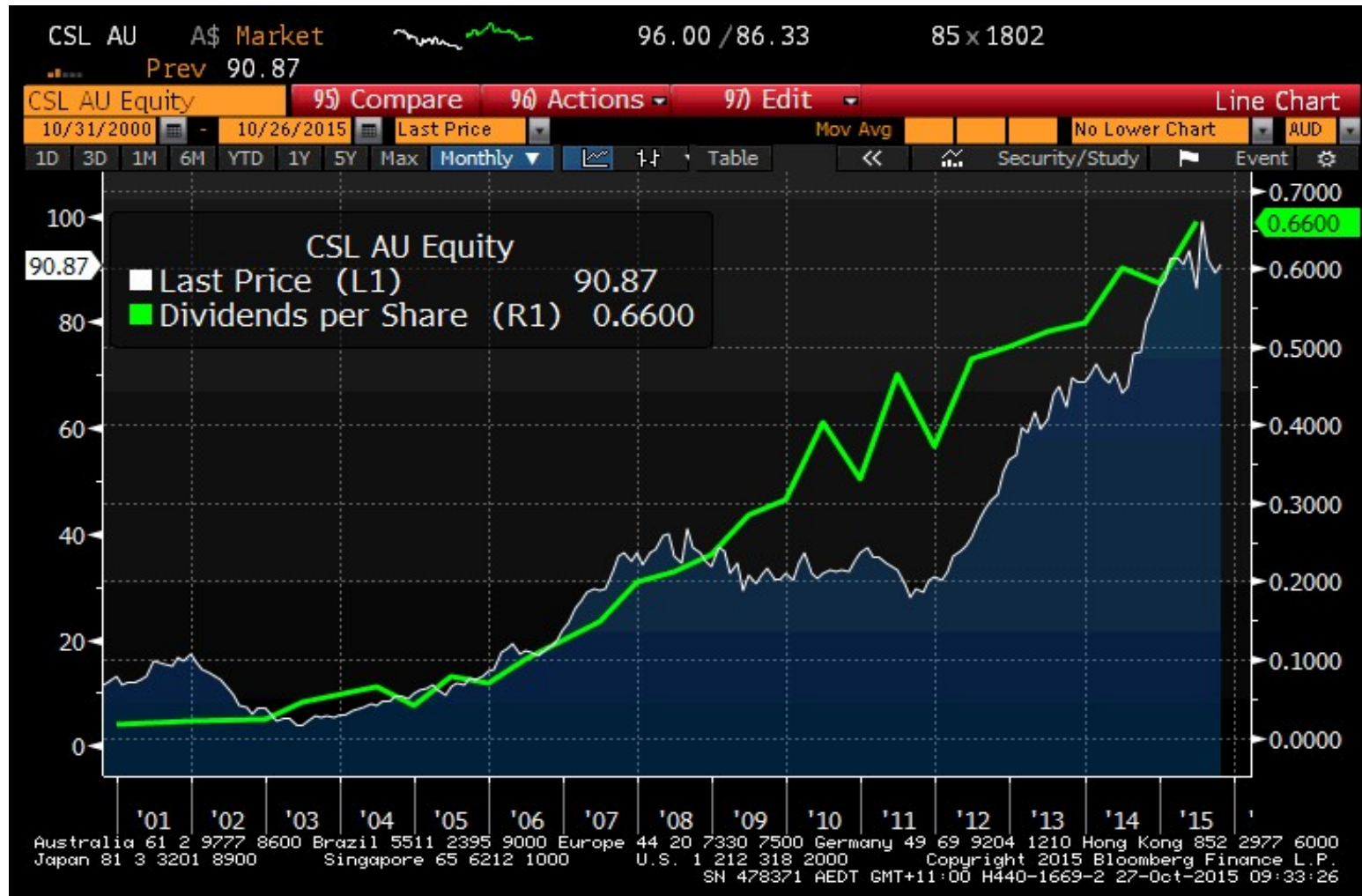
2015			
Price	\$9.63	\$5.52	\$92.44
Investment	\$3,006,250	\$117,697	\$1,016,942
Dividend	\$0.32	\$0.31	\$1.69
Yield	3.32%	5.53%	1.83%
Total Income	\$99,807.50	\$6,508.66	\$18,591.86

*excludes special

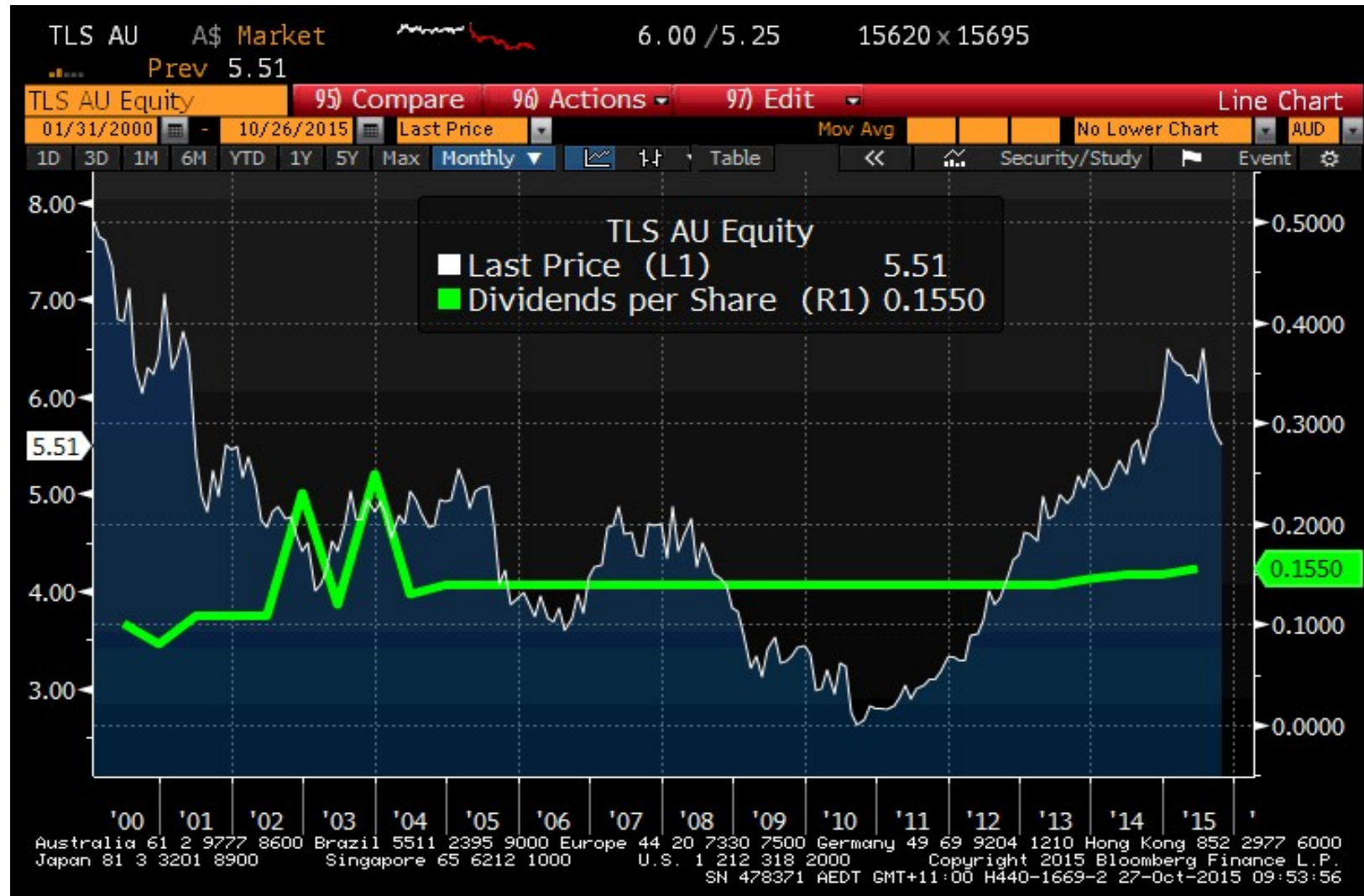
Growing Income in practice



Growing Income in practice



Growing Income in practice



ROE and Growth

The test

Has each dollar used to finance growth created more than a dollar of long term market value?

ROE and Growth

Value creation or destruction?

	Year 1	Year 2
Equity(b)	\$10.00	\$12.00
ROE	20%	20%
EPS	\$2.00	\$2.40
POR	0%	0%
DPS	\$0.00	\$0.00
Equity(e)	\$12.00	\$14.40
P/E	10	10
Price	\$20.00	\$24.00

	Year 1	Year 2
Equity(b)	\$10.00	\$10.50
ROE	5%	5%
EPS	\$0.50	\$0.53
POR	0%	0%
DPS	\$0.00	\$0.00
Equity(e)	\$10.50	\$11.03
P/E	10	10
Price	\$5.00	\$5.25

ROE and Growth

Other evidence

Fortune looked at 1000 of the largest stocks in the US:

Only 6 of the 1000 companies averaged over 30% ROE over the previous decade (1977-1986)

Only 25 of the 1000 companies averaged over 20% ROE and had no single year lower than 15% ROE

These 25 “business superstars were also stock market superstars” as 24 out of 25 outperformed the S&P 500 during the 1977-1986 period.

Last stat is valuable; Even in top performing backtests of low P/B or low P/E groups, 50-66% of stocks outperform the market not 96%.

Is Value being Created?

Not related to Price in the short term

BHP	\$b	\$b			
Year	2007	2016/17	Change	ROIE	Delta
Equity Contributed	4	5.4	1.4		35%
Profits Retained	32.6	67.1	34.5		106%
Borrowings	14.6	48.9	34.3		235%
Profit*	16.3	9	-7.3	-20.33%	-44.79%

*e2017

BHP AU/Equity	Ticker	Recall	Store		
xxx	User	Export			
Pricing Power		Weak			
Barriers to Entry			Below Average		
Industry Structure			Average		
Customer Stickiness		Weak			
Reliability of Demand			Below Average		
Growth Potential			Average		
Power v. Suppliers				Above Average	
Disruption Risk				Above Average	
Company Position					Superior
Capital Intensity/ ROIC			Average		
Other/ Not Covered			Average		

Is Value being Created?

Not related to Price in the short term

REA Group	\$m	\$m			
Year	2007	2016/17	Change	ROIE	Delta
Equity Contributed	56	97	41		73%
Profits Retained	11	584	573		5209%
Borrowings	8	0	-8		-100%
Profit*	15	253	238	38.76%	1586.67%

*e2017

BHP versus REA

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12 Month Price Performance Comparison



#Past performance is not indicative of future performance

BHP versus REA

MONTGOMERY



10 Year Price Performance Comparison



#Past performance is not indicative of future performance

Is Value being Created?

Reece Ltd

Years	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Reported Net Profit After Taxes (Millions)	\$ 100	\$ 114	\$ 96.73	\$ 114	\$ 119	\$ 113	\$ 119	\$ 123	\$ 166	\$ 192	
Normalised Net Profit After Taxes (Millions)	\$ 103	\$ 114	\$ 98.67	\$ 114	\$ 119	\$ 113	\$ 120	\$ 123	\$ 167	\$ 190	\$ 206
Total Shareholders Equity (Millions)	\$ 433	\$ 491	\$ 533	\$ 595	\$ 654	\$ 707	\$ 766	\$ 827	\$ 926	\$ 1,041	\$ 1,146
Return on Equity (%)	25.55%	24.58%	19.27%	20.20%	18.99%	16.67%	16.26%	15.46%	19.04%	19.28%	18.87%
Equity Left In (Millions)	\$ 422	\$ 481	\$ 523	\$ 585	\$ 644	\$ 697	\$ 755	\$ 816	\$ 915	\$ 1,029	\$ 1,067
Equity Put In (Millions)	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96	\$ 9.96
Shares On Issue (Millions)	99.60	99.60	99.60	99.60	99.60	99.60	99.60	99.60	99.60	99.60	99.60
Cash & Short Term Investments (Millions)	\$ 23.65	\$ 38.51	\$ 54.55	\$ 123	\$ 134	\$ 167	\$ 156	\$ 73.76	\$ 85.02	\$ 105	\$ 55.78
Total Debt (Millions)	\$ 5.21	\$ 31.77	\$ 47.79	\$ 8.96	\$ 8.30	\$ 9.02	\$ 8.89	\$ 205	\$ 175	\$ 145	\$ 120
Net Debt / Equity (%)	-4.26%	-1.37%	-1.27%	-19.11%	-19.24%	-22.31%	-19.24%	15.84%	9.73%	3.83%	8.97%

Is Value being Created?

Reece Ltd



Income & Value Creation.

Reece Limited



Is Value being Created?

ARB Ltd

Years	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Reported Net Profit After Taxes (Millions)	\$ 15.76	\$ 19.65	\$ 22.54	\$ 32.63	\$ 37.85	\$ 38.50	\$ 42.36	\$ 42.57	\$ 44.09	\$ 47.44	
Normalised Net Profit After Taxes (Millions)	\$ 15.71	\$ 19.50	\$ 22.33	\$ 32.65	\$ 37.70	\$ 38.15	\$ 42.12	\$ 42.45	\$ 43.96	\$ 45.88	\$ 50.26
Total Shareholders Equity (Millions)	\$ 68.83	\$ 77.73	\$ 92.04	\$ 111	\$ 129	\$ 151	\$ 178	\$ 198	\$ 226	\$ 250	\$ 273
Return on Equity (%)	24.19%	26.61%	25.84%	31.72%	31.33%	27.21%	25.63%	22.62%	20.62%	19.28%	19.24%
Equity Left In (Millions)	\$ 43.11	\$ 53.44	\$ 65.66	\$ 64.97	\$ 86.88	\$ 108	\$ 131	\$ 153	\$ 115	\$ 138	\$ 153
Equity Put In (Millions)	\$ 25.89	\$ 25.89	\$ 25.89	\$ 46.62	\$ 46.62	\$ 46.62	\$ 46.62	\$ 46.76	\$ 107	\$ 107	\$ 107
Shares On Issue (Millions)	66.57	66.57	66.57	72.48	72.48	72.48	72.48	72.49	79.16	79.17	79.18
Cash & Short Term Investments (Millions)	\$ 2.92	\$ 1.52	\$ 3.30	\$ 20.96	\$ 30.70	\$ 33.23	\$ 43.76	\$ 38.84	\$ 10.05	\$ 13.78	\$ 11.95
Total Debt (Millions)	\$ 9.81	\$ 10.01	\$ 1.50	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 2	\$ 0	\$ 0
Net Debt / Equity (%)	10.02%	10.92%	-1.96%	-18.81%	-23.74%	-21.98%	-24.65%	-19.63%	-3.56%	-5.52%	-4.59%

Is Value being Created?

ARB Ltd



Income & Value Creation.

ARB Limited



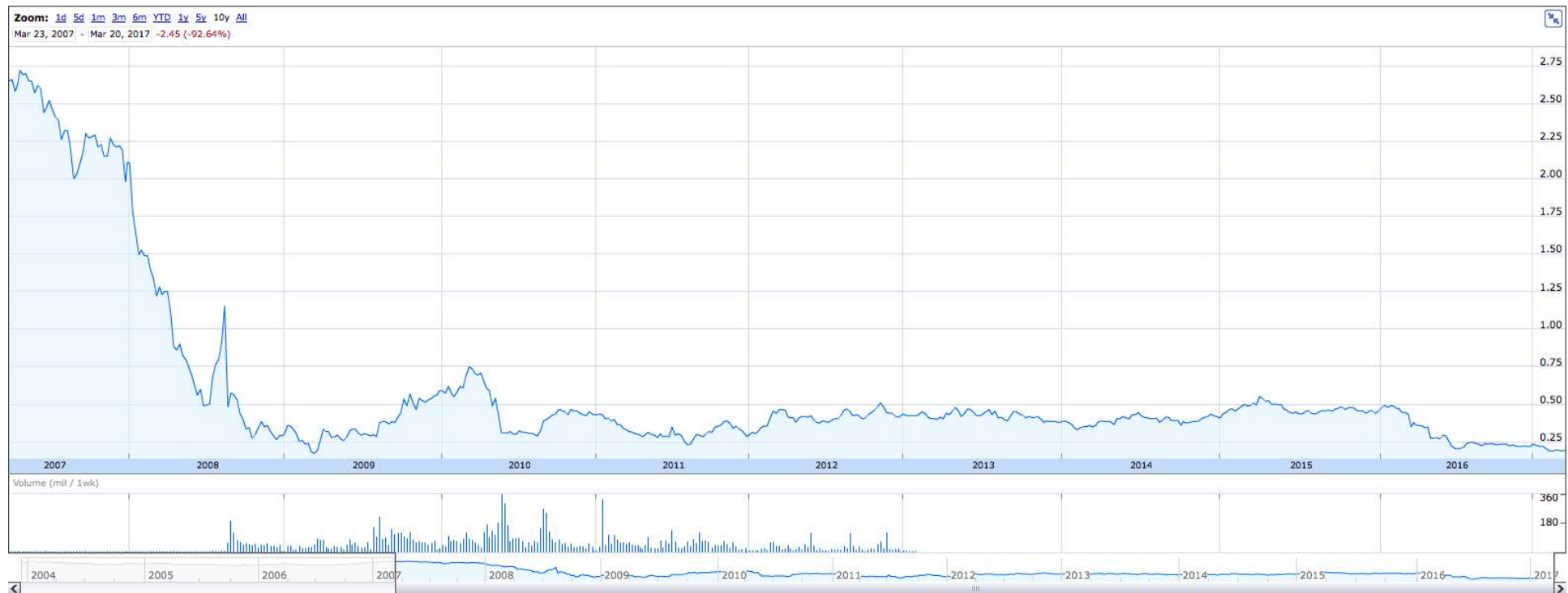
Is Value being Created?

Virgin Australia Holdings

Years	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Reported Net Profit After Taxes (Millions)	\$ 216	\$ 97.70	\$ -160	\$ 21.30	\$ -67.80	\$ 22.80	\$ -98.10	\$ -354	\$ -111	\$ -261	
Normalised Net Profit After Taxes (Millions)	\$ 220	\$ 98.67	\$ -180	\$ 27.08	\$ -64.94	\$ 43.76	\$ -96.80	\$ -249	\$ -51	\$ 25.43	\$ 38.06
Total Shareholders Equity (Millions)	\$ 744	\$ 925	\$ 577	\$ 933	\$ 926	\$ 930	\$ 1,101	\$ 1,048	\$ 1,077	\$ 912	\$ 2,139
Return on Equity (%)	32.42%	11.72%	-23.80%	2.98%	-6.98%	4.72%	-9.56%	-22.02%	-4.79%	2.71%	1.88%
Equity Left In (Millions)	\$ 398	\$ 458	\$ 297	\$ 303	\$ 236	\$ 260	\$ 229	\$ -124	\$ 61.40	\$ -251	\$ -290
Equity Put In (Millions)	\$ 405	\$ 406	\$ 408	\$ 633	\$ 633	\$ 633	\$ 795	\$ 1,147	\$ 1,153	\$ 1,309	\$ 2,244
Shares On Issue (Millions)	1,233.029	1,233.503	1,245.972	2,188.900	2,190	2,190	2,567.500	3,503.300	3,517.700	4,051.700	8,458.119
Cash & Short Term Investments (Millions)	\$ 704	\$ 604	\$ 476	\$ 815	\$ 737	\$ 811	\$ 593	\$ 813	\$ 1,089	\$ 1,156	\$ 1,649
Total Debt (Millions)	\$ 846	\$ 1,486	\$ 1,779	\$ 1,788	\$ 1,640	\$ 1,674	\$ 1,890	\$ 1,951	\$ 2,762	\$ 3,000	\$ 2,766
Net Debt / Equity (%)	19.15%	95.35%	225.87%	104.26%	97.50%	92.87%	117.74%	108.57%	155.43%	202.26%	59.62%

Is Value being Created?

Virgin Australia Holdings



Income & Value Creation.

Virgin Australia Holdings



Income & Value Creation.

BHP



Income & Value Creation.

REA



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<div>The Montgomery [Private] Fund</div> <div></div>	<div>The Montgomery Fund</div> <div></div>	<div>Montgomery Alpha Plus Fund</div> <div></div>	<div>The Montgomery <u>Global</u> Fund</div> <div></div>	<div>MONTAKA</div> <div></div>	<div>Montaka Global Access Fund</div>
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