Ironbark Karara Investment Funds

Quarterly Investment Report as at 31 December 2017

Market Review

Global equity markets maintained their strong momentum during the quarter with the MSCI World Index delivering a total return of 5.44% during the December quarter resulting in a total return of 20.6% during 2017. The key drivers being a positive scenario of synchronised global economic growth, tame inflation, a lower US dollar ('USD') and the successful passage of the Trump administration's tax reform bill. Commodity prices also rallied through the quarter, supported by strong Chinese import data. In this context, Australian equities performed strongly as the broad-based S&P/ASX 300 Accumulation Index rose 7.74% to close out the year 11.94% higher, while the small company index rose 13.69%, or 20.02% for the year.

The strong equity performance throughout 2017 has been underpinned by a broad-based acceleration in global economic growth. Goldman Sachs current activity indicator during November indicated global growth was running at approximately 5% year-on-year growth with developed markets having accelerated recently to approximately 3.9% year-on-year with all key economies (Europe, Japan and the US) contributing. Emerging market growth was approximately 6.5% year-on-year with China also around that level.

Unsurprisingly, strong economic growth has been a key contributor to stronger commodity prices than was broadly expected at the start of the year. The strength in commodity prices enabled the Australian equity markets to outperform global benchmarks with the S&P/ASX 300 Accumulation Index providing a total return of 7.74% over the December quarter. This represents a 2.3% outperformance compared to the MSCI World Index, albeit over 2017, it underperformed by approximately 8.7%.

Iron ore finished December at $74 per tonne (in USD terms) (62% FE, CFR China), which was a 20% increase from September. The high discounts for lower grade iron ore have continued, which means higher benchmark prices are not translating into a signal for lower grade marginal suppliers to increase production. The clear beneficiaries of this dynamic are the major iron ore producers (BHP and Rio) contributing to the metals & mining sector delivering a 15% return during the quarter.

Oil gained approximately 18% to finish at $67 per barrel (in USD terms) for Brent crude with data during the quarter clearly indicating inventories are well on their way to normalising. The combination of tighter inventories and ongoing OPEC discipline provide the space for US shale to maintain its growth through 2018, however the risk that the call on the US exceeds its growth capacity is increasing. Higher prices along with the prospect of large scale corporate activity (takeover approach to Santos) propelled the energy sector up 18%, which made it the top performing sector.

Ongoing evidence of a cooling property market and a disappointing results period lead to the banks being the largest underperforming sector (up 1.9%). Whilst the overflow is clearly coming out of the market, strong population growth (particularly from immigration) is assisting the absorption of the significant new supply of apartments.

Other underperforming sectors were utilities (up 3.2%) and the diverse industrials sector (up 5.5%).

Performance

Ironbark Karara Australian Share Fund

Fund size: $78.8 million **Exit Price: $1.6329** **Inception date: 30 June 2005**

	1 month (%)	3 months (%)	1 year (%)	3 years (pa) (%)	5 years (pa) (%)	7 years (pa) (%)	Since inception[3] (pa) (%)
Net Fund Return[1]	1.63	8.67	11.23	7.49	9.50	7.68	6.87
Benchmark[2]	1.86	7.74	11.94	8.76	10.15	8.13	7.48
Excess Return	-0.23	0.93	-0.71	-1.27	-0.65	-0.45	-0.61

Ironbark Karara Australian Small Companies Fund

Fund size: $655.1 million **Exit Price: $3.7278** **Inception date: 30 June 2005**

	1 month (%)	3 months (%)	1 year (%)	3 years (pa) (%)	5 years (pa) (%)	7 years (pa) (%)	Since inception[3] (pa) (%)
Net Fund Return[1]	2.89	11.63	19.18	11.02	10.53	8.52	13.76
Benchmark	3.20	13.69	20.02	14.38	7.39	2.59	4.71
Excess Return	-0.31	-2.06	-0.84	-3.36	3.14	5.93	9.05

Past performance is not an indicator of future performance. Net performance figures are calculated using exit prices, net of fees and reflect the annual reinvestment of distribution. Retail investors should refer to net returns. If investing through an IDPS Provider, the total after fees performance return of your investment in the Fund may be different from the information in this report.

[1]Karara Capital appointed investment manager on 1 May 2010, Fund performance prior to this date is not attributable to Karara Capital but the prior manager.

[2]The S&P/ASX 300 Accumulation Index was adopted as the Fund's performance benchmark on 1 July 2010. Benchmark calculations prior to this date are based on the S&P/ASX All Ordinaries Index.

[3]This figure represents the annualised performance of the Fund since inception.

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Ironbark ASSET MANAGEMENT

Market Review (cont'd)

Versus a backdrop of strong global growth, Australia's economic growth remains relatively modest albeit it has accelerated of late partially underpinned by strong population growth and the significant step up in infrastructure investment underway. The missing ingredient remains stronger levels of business investment, which remains relatively subdued.

Strong employment growth continued throughout the quarter. Over the last three months (September to November) employment growth and hours worked has been 3.1% year-on-year, which is the fastest pace since 2008. The sectors that have made the strongest absolute contributions to growth are the health care and social assistance sector and the construction sector. Collectively they have contributed approximately 55% of the net growth in employment (384 thousand people) over the last 12 months. Unsurprisingly, the manufacturing sector with the recent shutdowns of car manufacturing in Australia has seen a 9% decline in employment detracting 84 thousand jobs over the same period. Unexpectedly, despite the prevailing gloom over the retail sector (the second largest sector by employment), employment has grown by approximately 5% year-on-year.

Whilst employment growth has been strong, this has yet to translate into higher wages, which remains around 2% year-on-year growth. The slack in the labour market has been able to absorb faster job creation, however this slack is decreasing rapidly and with ongoing strong vacancies and job advertisements, faster wages growth remains likely over the coming 12-18 months. Combined with ongoing employment growth, this should underpin consumer spending despite the recent weak patch.

The lack of wages growth and benign inflation in Australia resulted in the Australian 10-year government bond yield declining by 20 basis points to 2.66% supported by the market reducing the prospect of the Reserve Bank of Australia ('RBA') rate hikes during 2018 with around 20 basis points now priced in.

US economic data maintained its momentum with employment growth continuing and other measures remaining strong. As a result, the Federal Reserve ('Fed') raised their target range for Fed Funds to 1.25-1.5% at their December meeting. Interest rate markets now have approximately 50 basis points of rate hikes priced during 2018 versus the median expectation of the members of the Federal Reserve board of 75 basis points.

Global bond yields marginally increased with US 10-year government bond yields increasing by 12 basis points to 2.43%. This meant the spread between Australian and US yields sharpened materially by 32 basis points, which more than reversed the previous quarters widening of 21 basis points. The narrowing of yields didn't translate into a material change in the exchange rate with the Australian dollar ('AUD') against the US dollar staying flat at $0.78 AUD/USD. However, the Australian dollar weakened against both the Euro and the British Pound during the quarter by approximately 2%.

The dispersion between highest and lowest rated stocks continues to widen. The top quintile of the largest industrial companies (which has a median one year forward price-to-earnings ratio ('PE') of 30.2 times) has rallied 14.4% over the last three months. By contrast the lowest quintile, with a forward of PE 13.1 times, is up only 4%. This has not been driven by differential earnings performance. The higher quintile group has seen median earnings estimates up 1% while the 'cheap' stocks have been flat.

Portfolio Performance & Portfolio Activity

Ironbark Karara Australian Share Fund

The Ironbark Karara Australian Share Fund (the 'Fund') increased 8.67% (net) during the December quarter. This constituted an outperformance of 0.93% when compared with the S&P/ASX 300 Accumulation Index return of 7.74% (net) for the quarter.

Energy positions, particularly Santos (up 36%) and Origin (up 26%), were the strongest contributors. They benefitted from both the improvement in the oil price but also the actual and the potential for further strong productivity improvements in their respective coal seam gas LNG projects. Santos was also assisted by another takeover approach. Whilst the investment manager does not have a high expectation that Harbour Energy, backed by EIG Global Energy Partners, will produce an acceptable bid, they do think that perceptions around the quality of Santos's assets have been permanently revised higher. The threat of a low bid gaining traction is likely to make management more inclined to spell out the implications for future growth and dividends.

The Fund's position in Oil Search (up 11%) was added to following share price weakness after their surprise $400 million (in USD terms) acquisition of an Alaskan development project. Although the project looks attractive, Oil Search was not short of organic growth options and this move pushes out and re-risks future cash flows.

The gains from energy producers were partially offset by Qantas (-14%), although they finished the year up 51%. Concerns around oil price sensitivity and uncertainty around international capacity additions provided the excuse for abrupt profit taking. The investment manager believes an improved domestic market structure will reduce sensitivity to these factors going forward and that current earnings will be broadly sustained, or rise if current demand conditions are maintained. This is still not reflected in the price. The position, which had been reduced, has been partially rebuilt following weakness.

James Hardie's (up 28%) second quarter results showed very strong unit cost improvement, better-than-expected price outlook and confident statements that lost customers were returning supporting the confidence that the issues faced earlier this year are behind them. The company was also refreshingly direct with their rationale for acquiring Fermacell, a European producer of a niche sound and fire resistant plasterboard product. Hardie's paid a full price for a good business but believes it has the brand and distribution strength to meaningfully establish Hardie's fibre cement siding in Europe.

Portfolio Performance & Portfolio Activity (cont'd)

Star (up 16%) and Crown (up 15%) gave annual general meeting updates in October that showed VIP play is returning much more quickly than the market had anticipated. Star trading was flat relative to the prior period (which was not impacted by the arrests in China) while Crown's VIP activity was down only 17% whereas it had been 57% lower in the six months to June. Crown also announced a series of transactions in December regarding non-core assets that will aid in strengthening its balance sheet during the development of Crown Sydney at Barangaroo.

Strong stock selection also assisted with other portfolio holdings, Navitas (up 20%), Resmed (up 13%) and Brambles (up 12%) were all key contributors. The position in Navitas was reduced given the recent strength seems largely attributable to broader market factors.

Underweights in Bluescope (up 40%) and Westfield (up 21%) were amongst the top detractors. Bluescope benefitted from higher steel spreads emanating from China and Westfield agreed to a takeover by European mall operator, Unibail-Rodamco, with the merged entity to remain listed on the ASX post completion of the transaction.

The Fund's small overweight position to the major banks detracted during the quarter. Also underperforming was AGL (up 4%) despite the recent policy announcements from Federal and Victorian governments that have materially reduced the risk of a negative intervention in the National Electricity Market.

The position in Clydesdale (up 13%) was increased post their result in late November. The investment manager views it as a cost and capital self-help story coupled with leverage to UK base rate increases underpinned by reasonable valuation parameters and strong forecast earnings per share growth.

Ironbark Karara Australian Small Companies Fund

The Ironbark Karara Australian Small Companies Fund (the 'Fund') rose 11.63% (net) during the December quarter. This constituted an underperformance of 2.06% when compared with the S&P/ASX Small Ordinaries Accumulation Index return of 13.69% (net) for the quarter.

The strongest contributors to Fund performance at a sector level were underweight positions in Property Trusts and Consumer Discretionary. Overweight positions in Information Technology and Utilities detracted.

At a stock level, positive contributors to quarterly performance included overweight positions in Elders, AWE, Altium and Saracen Minerals. An underweight position in Retail Food Group also contributed. Shares in Elders rose 73% after the company's 2017 financial year result beat expectations on all metrics, highlighting strong cash conversion, a solid balance sheet and the first dividend payment since 2008. Shares in AWE rose 31% after the company received several competing bids from both China Energy Reserve and Chemical Group ('CERCG') and Mineral Resources. At the time of writing Mineral Resources had submitted the highest bid price by proposing an all-scrip transaction with an implied value of $0.83, compared with CERCG's offer of $0.73. However CERCG received approval from the Foreign Investment Review Board late in December, potentially paving the way for a higher bid. As a result AWE shares ended December at $0.88. Altium shares gained 23% after the company released an update to its business strategy that reinforced its medium-term growth ambitions remain on track. Saracen shares added 29% on little news but a stronger gold price.

The largest detractors to quarterly performance included overweight positions in G8 Education, Australian Agriculture and Technology One. Shares in G8 lost 17% after the company reported softer occupancy and rising costs. Australian Agricultural shares fell 15% following an underwhelming first half 2018 result that showed the company had made only modest progress in its 'premiumisation' strategy in the wake of management changes. Technology One ended flat for the quarter after the company reported a 2017 financial year result that was behind expectations.

Top 5 Active Weights

Ironbark Karara Australian Share Fund

Security Name	Sector	% of Fund
CSL	Health Care	-3.85
AGL Energy	Utilities	3.45
Origin Energy	Energy	2.95
Brambles	Industrials	2.67
Telstra Corporation	Telcomm. Services	-2.60

Ironbark Karara Australian Small Companies Fund

Security Name	Sector	% of Fund
Altium	Information Technology	4.27
Costa Group Holdings	Consumer Staples	3.47
Bega Cheese	Consumer Staples	3.20
Technology One	Information Technology	2.54
Saracen Mineral Holdings	Materials	2.44

Ironbark Karara Investment Funds

Quarterly Investment Report as at 31 December 2017

Market Outlook

Global growth indicators remain robust, although inflationary expectations currently remain modest. The investment manager anticipates above-trend global growth to continue for some time and for slack in the global economy to decline resulting in higher rates of inflation in due course. With the durability of this period of growth doubted by many market participants, large pools of global capital remain defensively positioned.

Slack in the US economy and labour market is now relatively low and rapidly decreasing in Europe and Japan. Given this, the significant expansionary monetary policy pursued by the three key central banks is increasingly less appropriate and risks are rising that the market is underestimating the pace of tightening that may be required. However, the investment manager anticipates that the key central banks will have some tolerance around inflation exceeding their targets as wage inflation picks up

With the global earnings outlook improving and a decent gap between earnings and bonds yields, there is scope for the stock market to weather somewhat higher interest rates. The key macro risks remain twofold:

- The sustainability of debt driven Chinese growth. Given the success of 2016's stimulatory efforts, the Chinese Government's focus has moved judiciously towards containing risks, controlling credit growth and advancing reform. The investment manager expects policy to be more modulated going forward and overall less supportive for steel making materials.

- The structural challenges in Europe remain unresolved. Better growth and recent electoral outcomes are encouraging however adverse political risks remain.

Whilst the global growth improvement is relatively synchronised, Australia is lagging. The investment manager anticipates that Australian gross domestic product ('GDP') growth will remain modest at around 2-3%. Strong population growth is assisting headline growth numbers with per-capita growth quite low in a historical context.

The recent pickup in domestic economic data is encouraging, particularly the recent employment data. Overall, the investment manager expects aggregate consumer spending to be broadly in line with household income growth (3-4%), which is still low in a historical context. Further strength in the Australian dollar could jeopardise this.

House prices are high by any measure and conditions in the housing market vary considerably outside of Melbourne and Sydney. The tightening of credit to the investor segment of the market has had a cooling impact on the housing market with a reasonable likelihood of small real price declines over the next couple of years. As a small open economy, the key risk to house prices remains external macro shocks which have, if anything, diminished of late.

Moderate global growth and the return of pricing power in some sectors suggest a reasonable backdrop for many stocks. Although, after the expansion in valuations in recent years, sustained gains will require continuing profit delivery.

The high-levels of valuation dispersion that were observed last year have returned, and exceeded, driven by ongoing increases in the valuations of stocks with defensive growth characteristics. This group of stocks now trades at historically high valuation levels and the Fund remains underweight to this area.

The Fund remains generally positioned for a more reflationary environment than is currently priced by the market and the investment manager continues to believe there are good risk adjusted returns available in many sectors. Within this, the emphasis is on attractive quality companies whose prospects are unappreciated by the market.

Key Contributors & Detractors over the Quarter

Ironbark Karara Australian Share Fund

Top 5 Contributors	Active Position
Santos	Overweight
Origin Energy	Overweight
James Hardie Industries	Overweight
Navitas	Overweight
Star Entertainment Group	Overweight

Top 5 Detractors	Active Position
Qantas Airways	Overweight
Bluescope Steel	Underweight
ANZ Banking Group	Overweight
Westfield Corporation	Underweight
AGL Energy	Overweight

Ironbark Karara Australian Small Companies Fund

Top 5 Contributors	Active Position
Elders	Overweight
AWE	Overweight
Saracen Mineral Holdings	Overweight
Altium	Overweight
Dacian Gold	Overweight

Top 5 Detractors	Active Position
G8 Education	Overweight
Australian Agricultural Company	Overweight
Technology One	Overweight
Pilbara Minerals	Overweight
Mercury NZ	Overweight

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Ironbark ASSET MANAGEMENT

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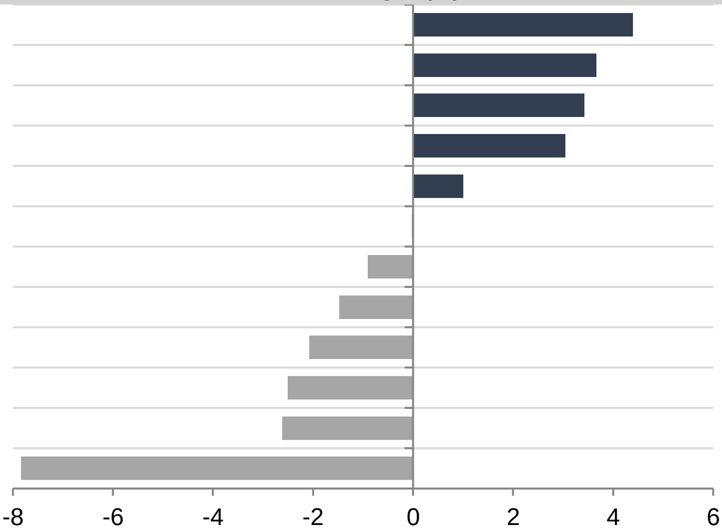
Asset Allocation

Ironbark Karara Australian Share Fund

Sector Weights	Fund (%)	Bench (%)
Energy	9.58	5.19
Materials ex Metals & Mining	7.76	4.09
Consumer Discretionary	8.28	4.86
Utilities	5.07	2.02
Industrials	8.38	7.37
Information Technology	2.04	2.07
Health Care	6.16	7.07
Consumer Staples	5.99	7.47
Financial ex Property Trusts	32.89	34.97
Telecommunications Services	0.54	3.04
Metals & Mining	11.03	13.64
Property Trusts	0.37	8.21
Cash	1.91	0.00

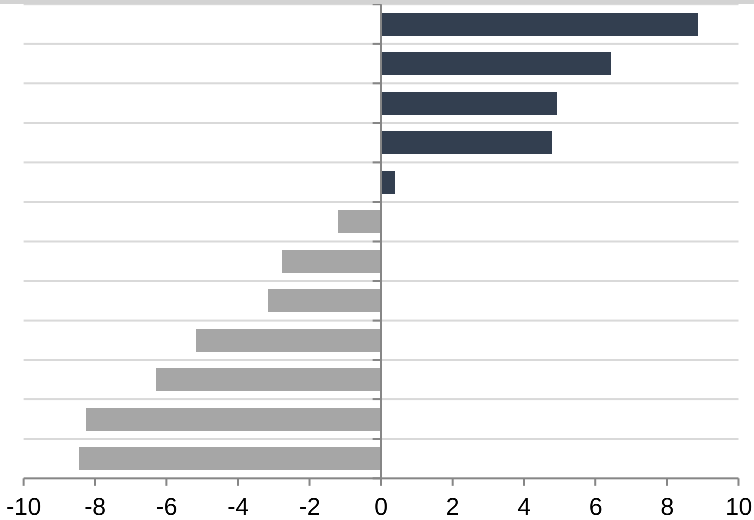
Active Weight (%)



Ironbark Karara Australian Small Companies Fund

Sector Weights	Fund (%)	Bench (%)
Information Technology	17.24	8.37
Consumer Staples	14.87	8.45
Utilities	5.45	0.53
Metals & Mining	20.85	16.08
Financial ex Property Trusts	8.59	8.20
Telecommunications Services	0.63	1.83
Energy	4.53	7.30
Materials ex Metals & Mining	0.00	3.16
Health Care	1.41	6.60
Industrials	3.51	9.80
Consumer Discretionary	9.86	18.12
Property Trusts	3.11	11.56
Cash	9.95	0.00

Active Weight (%)



Important Information

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