

# NAOS Emerging Opportunities Company (NCC)

NAOS

## MONTHLY INVESTMENT REPORT AND NTA UPDATE

July 2016

### KEY CHARACTERISTICS

#### 1. Genuine Exposure to Undervalued Emerging Companies

Regardless of market capitalisation and/or liquidity, NCC seeks to provide investors with exposure to high quality, undervalued emerging companies in a transparent and concentrated structure that has the competitive advantage of being a nimble closed ended fund with no liquidity constraints.

#### 2. Focus on Quality of Companies Not Quantity or Size of Companies

Our primary focus is on developing a deep understanding and appreciation of the companies in our portfolio. We believe the best way to achieve this is to focus on a select number (target 0-15) of high quality investment ideas. By developing a deep understanding of these companies we believe we are well positioned to capitalise on our 'long term information advantage' & 'liquidity advantage'.

#### 3. Focus on Meaningful Long Term Performance

We target an Internal Hurdle Rate of 20% p.a. over a rolling three-year period for all our investment holdings.

#### 4. Portfolio Constructed Utilising a Benchmark Unaware Approach

Being benchmark unaware means we are not forced holders of stocks with large benchmark weightings that we are not convinced are attractive investment propositions.

#### 5. Significant Alignment of Interests with Shareholders

NAOS & NCC employees/directors own >10 million NCC shares, providing shareholders with a significant alignment of interests.

### Net Tangible Asset Value Breakdown as at 31<sup>st</sup> July 2016

Pre Tax NTA:	\$1.30
Post Tax & Pre Unrealised Gains NTA:	\$1.32
Post Tax NTA:	\$1.22

**\*\*A gentle reminder that NAOS will be holding our inaugural semi-annual investor roadshow presentations in Sydney, Melbourne, Brisbane, Adelaide and Canberra. The presentation is open to current and prospective shareholders though RSVP is essential for catering requirements so please register your attendance at [enquiries@naos.com.au](mailto:enquiries@naos.com.au)**

### Investment Portfolio Performance to 31<sup>st</sup> July 2016 & Market Insight

The NCC investment portfolio produced a positive return of +4.63% for the month of July compared to the benchmark Small Ordinaries Accumulation Index (XSOAI) which increased by a not so insignificant +8.57%.

Within the portfolio there were a couple of significant releases made by one of the largest positions within the NCC portfolio, BSA Limited (ASX: BSA). Firstly, BSA announced that for FY16 the underlying EBITDA result would be slightly lower than FY15 mainly due to the timing of a number of new project wins that will fall within FY17 and FY18 coupled with the costs associated with resourcing for these contracts occurring in FY16. Significantly, post this release BSA also announced that it has been awarded its 2<sup>nd</sup> contract with NBN Co. This is a very significant announcement as it marks the 2<sup>nd</sup> contract win with NBN Co and in our view sets BSA up with a potential revenue base from NBN alone in the region of circa \$200 million at margins that should be higher than the current group profile. Given the current revenue base of BSA is circa \$500 million this is not an insignificant outcome.

When reviewing the basic BSA investment fundamentals over a 24-month period we believe that the current revenue base has the potential to increase to circa \$700 million from the current \$500 million. When comparing to margins of listed peers such as Service Stream (ASX: SSM), whose last release EBITDA margin was ~7.50%, this illustrates the opportunity for BSA which had an underlying FY16 EBITDA margin for BSA of ~3.2%. We do not necessarily believe that 7% is a realistic goal for BSA over the long term but when factoring in the recent contract wins and the significant change within revenue profile of the business we believe an EBITDA margin of 4.5% - 5.0% is achievable over the long term. With a large net cash balance sheet and a significant franking balance NAOS believe BSA still makes a compelling long term investment opportunity.

	1 Month	6 Months	1 Year	2 Years (p.a.)	3 Years (p.a.)	Inception (p.a.)	Inception (nom.)
NCC Investment Portfolio Performance*	+4.63%	+26.62%	+27.65%	+13.76%	+16.84%	+21.12%	+92.76%
S&P/ASX Small Ordinaries Accumulation Index (XSOAI)	+8.57%	+22.34%	+22.29%	+9.04%	+8.71%	+4.75%	+17.25%
Outperformance Relative to Benchmark	-3.94%	+4.28%	+5.36%	+4.72%	+8.13%	+16.37%	+75.51%

\*Investment Portfolio Performance is post all operating expenses, before fees, taxes and initial IPO and placement commissions. Performance has not been grossed up for franking credits received by shareholders. Since inception (p.a. and nom.) includes part performance for the month of February 2013.

**Positive Stock Attribution Analysis**  
 (Attribution is what has contributed to NCC's performance since inception)  
 (1st March 2013 to 31st July 2016)

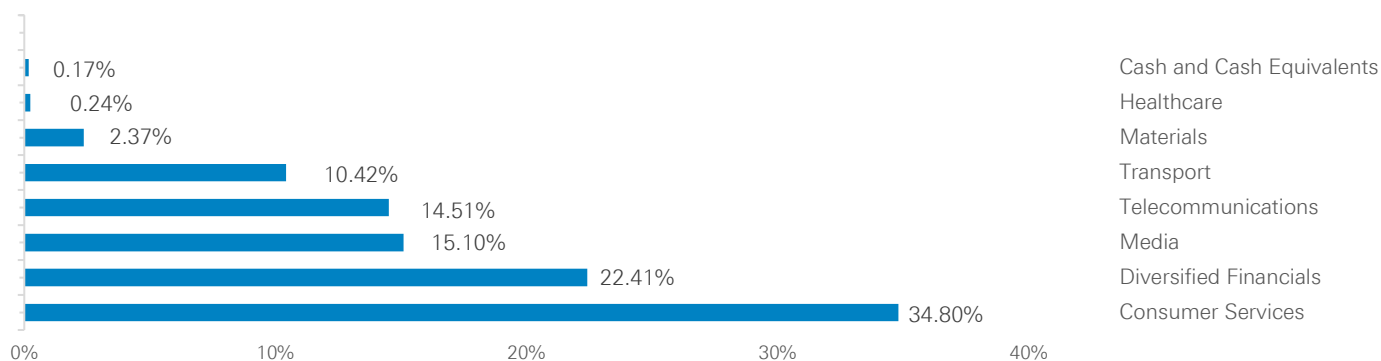
The table below lists the top positive contributors to NCC's total return since 1st March 2013. The purpose of the information is to illustrate that the performance the investment team derive over time is not simply from one or two positions but from a variety of positions, even with a highly concentrated portfolio of investments that is often 0 -15 securities at any one time. We will disclose securities in which the Company has a current substantial holding, or when we have exited the position. All of the below have **either been a long or short position** in the portfolio at some point in time.

Investment	Contribution to Return (%NAV)	Investment	Contribution to Return (%NAV)
BSA Limited	+19.63%	Village Roadshow Limited	+7.44%
Calliden Group	+14.04%	Sirtex Medical Limited	+7.43%
Capitol Health Group	+13.65%	RHG Limited	+6.38%
Armidale Investments	+12.30%	Gage Road Brewing	+5.61%
Lindsay Group	+10.70%	Enero Group	+5.07%
Tamawood	+7.82%	AMA Group	+3.96%

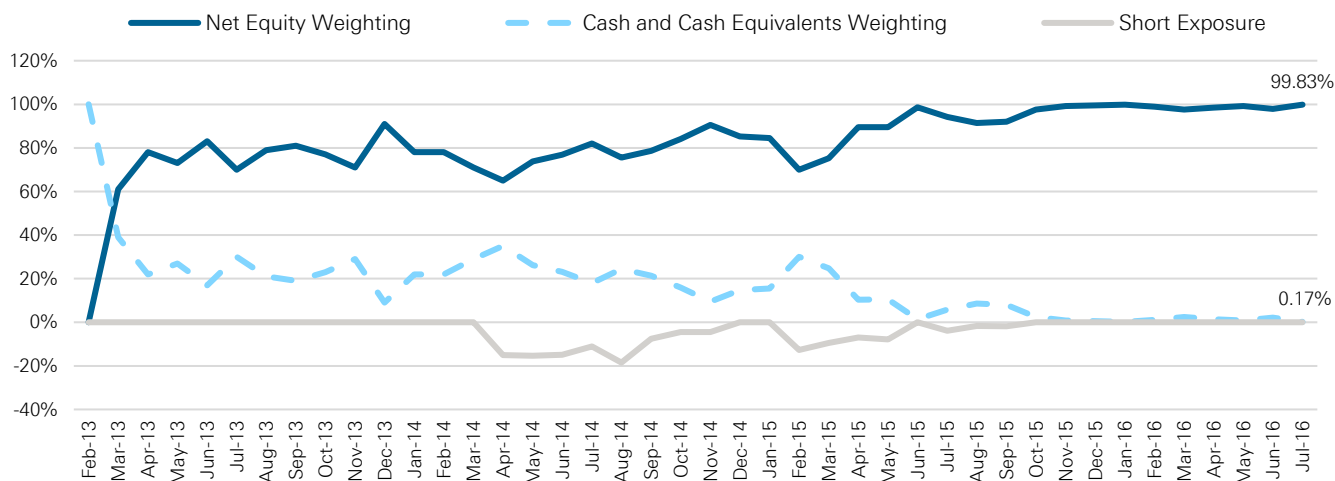
**Portfolio Positioning as at 31st July 2016**

As at July month end, the portfolio's net equity exposure was ~98% with a subsequent cash weighting of +0.17%. The core holdings in the portfolio did not change over the course of the month. As at month end, the portfolio was comprised of 9 long positions and no shorts. There were also no income instruments in the portfolio.

**Industry Exposure**



**Net Equity Exposure**



## Company Meetings

The NAOS investment philosophy is based around the belief that for an emerging company to succeed and generate strong returns for shareholders it must be led by a motivated, proven and experienced management team. This is why the NAOS Investment Team has direct contact with many listed and unlisted emerging companies across a wide range of industries. A selection of the companies we met with during the month of July is provided below.

- Austin Engineering – (ANG)
- BSA Limited – (BSA)
- Over the Wire – (OTW)
- Pacific Environmental – (PEH)
- Carbine – (CRB)
- XRef – (XF1)
- Promedius – (PME)
- Quantum – (IPO)
- Armidale Investment Corp – (AIK)
- Oroton – (ORL)
- Contango Limited – (TDX)
- Family Zone – (IPO)

## Portfolio Characteristics – Summary Data

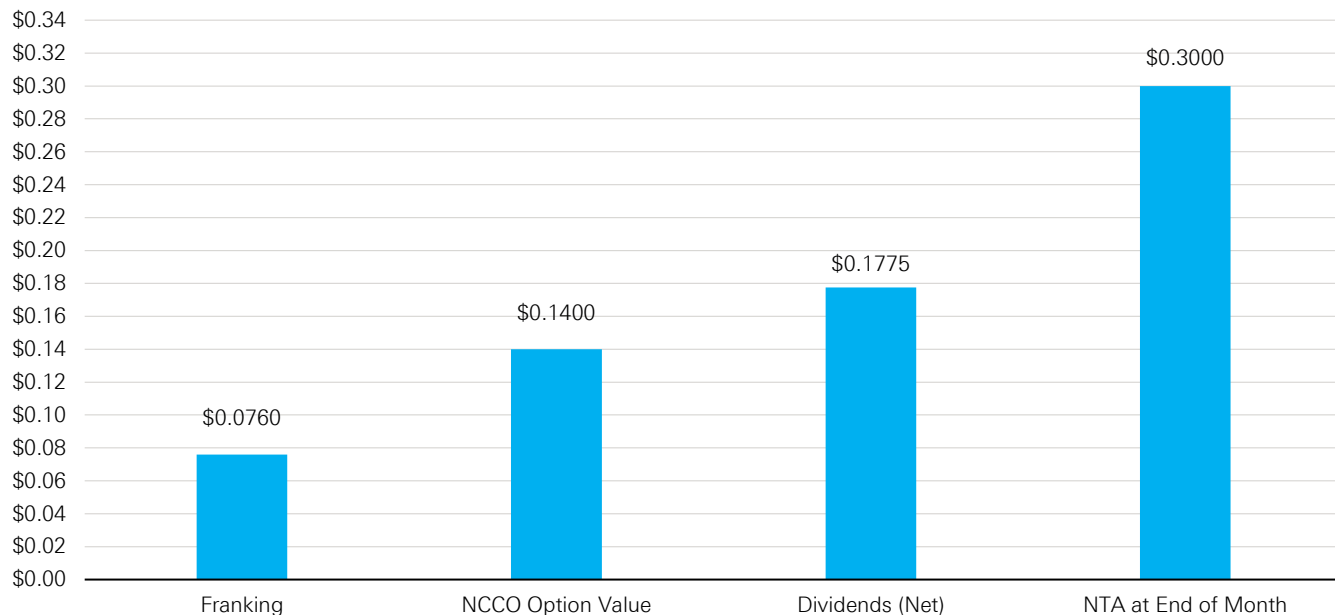
Below are a number of historical portfolio risk measures. Our aim in providing these metrics is to demonstrate to investors how NCC is placed from a risk adjusted basis to meet its objective, being to outperform the benchmark over the long term, and also to preserve investor's capital. A glossary of the terms used below and the method used for calculating them can be found on the last page of this report.

Portfolio Weighted Average Market Capitalisation	\$120 Million
Percentage of Positive Months (NCC)	76%
Percentage of Positive Months (XSOAI)	57%
Standard Deviation of Returns (NCC)	11.48%
Standard Deviation of Returns (XSOAI)	14.76%
Correlation of Returns to XSOAI	0.61
Sortino Ratio	3.13
Downside Deviation (NCC)	5.93%
Downside Deviation (XSOAI)	7.57%
Current Estimated Portfolio Beta (6 Month Historical)	-0.05

## Capital Management – Summary Data as at 31<sup>st</sup> July 2016

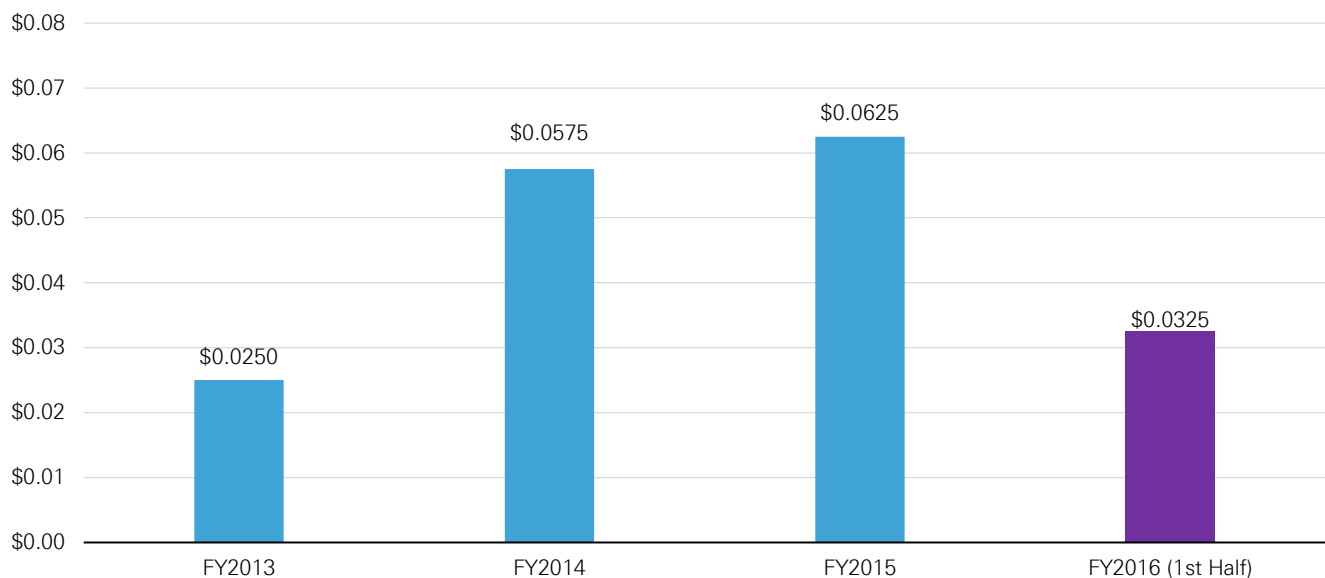
Share Price	\$1.15
Discount/Premium to NTA (Pre-Tax)	-11.54%
Historical Fully Franked Dividend Yield	5.43%
Historical Gross Dividend Yield	7.75%
Shares on Issue	46,918,297
NCC Directors Shareholding (Ordinary Shares)	3,540,066

### Historical Shareholder Return Breakdown



\*Assumes an intrinsic NCCO value of \$0.14 cents per option at expiry (1st February 2015).

### Dividend Profile - Historical Fully Franked Dividends (Cents per Share)



## Description of Statistical Terms/Glossary

**Portfolio Average Market Capitalisation** – The portfolio weight of each individual position multiplied by each company's respective market capitalisation.

**Standard Deviation of Returns** – A historical analysis of the volatility in monthly returns also known as historical volatility.

**Correlation of Returns** – A statistical measure of how two variables move in relation to each other. In this case the two variables are NCC and XSOAI. If the correlation is 1 then the two securities should have the same monthly returns and if the correlation is -1 and XSOAI had a return of -1.00% then NCC would be expected to have a return of +1.00%

**Sortino Ratio** – A modification of the Sharpe ratio that differentiates harmful volatility from general volatility by taking into account the standard deviation of negative asset returns, called downside deviation. A large Sortino Ratio may potentially indicate that there is a low probability of a large capital loss. Returns less than that of the benchmark (Small Ordinaries Accumulation Index - XSOAI) are classified as negative asset returns.

**Downside Deviation** - A measure of downside risk that focuses on returns that fall below a minimum threshold or minimum acceptable return (MAR). For our calculations, we use returns negative to zero for the calculation of portfolio downside deviation.

**Portfolio Beta** – A measure of the volatility, or systematic risk of a portfolio or security. A beta of 1 indicates a portfolio/security's price will move with the market. A beta of less than 1 indicated that a security/portfolio should be less volatile than the market.

**XSOAI** – Small Ordinaries Accumulation Index

### Disclaimer:

This report has been prepared by NAOS Asset Management Limited. Information provided in this report is for general information purposes and must not be construed as investment advice. In preparing this report we have not taken into account the investment objectives, financial situation or needs of any particular investor. Past performance is not a reliable indicator of future performance. Before making an investment decision, investors must read the offer documents and should seek their own financial product advice. Returns are compounded for periods greater than 12 months. The Investment Manager of the Company is NAOS Asset Management Limited (ABN 23 107 624 126, AFSL 273529). NAOS Address: Level 34, MLC Centre, 19 Martin Place, Sydney NSW 2000.

### CORPORATE DIRECTORY

#### Directors

David Rickards (Independent Chairman)  
Warwick Evans (Director)  
Sebastian Evans (Director)

#### Company Secretary

Richard Preedy

#### Investment Team

Sebastian Evans (Chief Investment Officer)  
Jeffrey Kim (Portfolio Manager)  
Robert Miller (Portfolio Manager)  
Ben Rundle (Portfolio Manager)  
Chadd Knights (Investment Analyst)

#### Chief Financial/Operating Officer

Richard Preedy

#### Business Development Manager

Julia Stanistreet

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Facsimile: 1300 653 459

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Sydney NSW 2000

#### Registered Office

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#### ENQUIRIES

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