

SPECIALIST SMALL COMPANIES INVESTMENT MANAGER

March 2016



GLENNON CAPITAL

ABOUT GLENNON CAPITAL

**Established in 2008
as a specialist
small companies
investment manager**

**Focused on
finding value
in small listed
companies**

**Undertake
our own
research**



**Extensive small company
experience in investing,
along with extensive
contacts among small
listed companies**

**Only invest in quality
business; it's as much
about avoiding the
disasters as picking
winners.**

**Co-investment. We back
our own investment
decisions and have
our funds invested
alongside our clients**

OUR VALUES

**We want to add
absolute value**

**We want to
be aligned
with our clients**

**We want our
investment to grow
with our client's
investments**

**We want to
communicate
with our clients so they
have confidence in our
capability and to reassure
them when markets
are volatile**

**We want to
think creatively
and outside
the box**

**We want to
be long term
and look through
the noise**

INVESTMENT PHILOSOPHY

We believe the market shows varying degrees of inefficiency

We add value by concentrating our research efforts in areas where inefficiencies exist

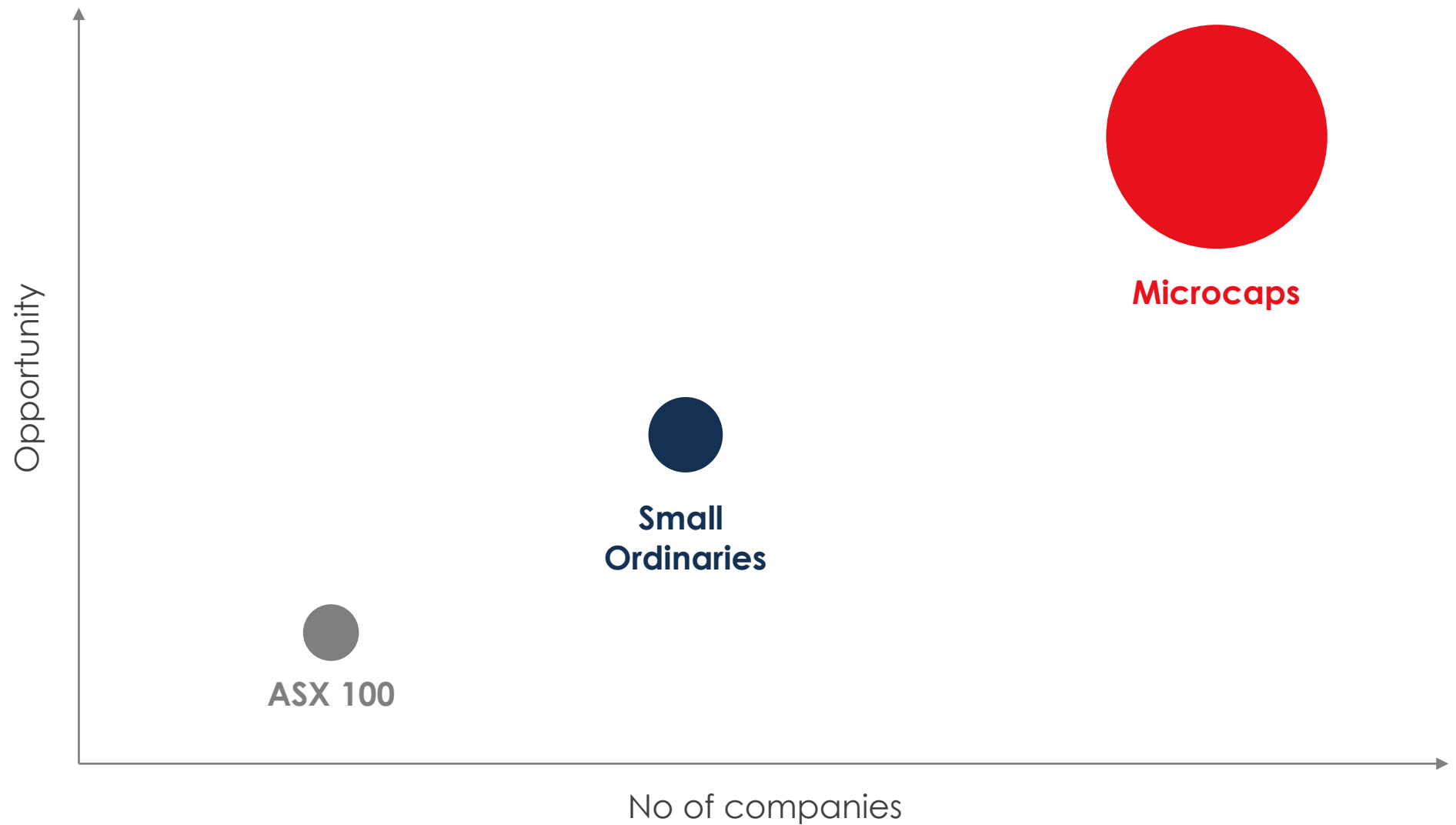
We have found that larger companies tend to have better information flows, and as a result their prices tends to better reflect publicly available information

Smaller companies are not subject to the same structural information flows, providing greater opportunities to find value

There are more opportunities in smaller companies because they are far greater in number and there are structural inefficiencies in terms of the information readily available to investors

We take the view the we are buying businesses and that we are an owner of the business

WHY SMALL CAPS?



PEOPLE

INVESTMENT CREDENTIALS



Michael Glennon
Portfolio Manager

- 17 years experience in financial markets
- 15 years as a specialist small cap manager
- Regular media appearances commentating on financial markets
- Small companies Portfolio Manager (previously Adam Smith, Paradise, Soul Pattinson)
- Previously ran the listed investment company Pacific Strategic Investments, which was acquired by Brickworks Investment Company
- Small companies Credit Analyst (ANZ), Wholesale Investment Management (ING IM)

17 years experience in financial markets and over 15 years experience as a portfolio manager and director of several boutique investment management firms. Michael is one of the most experienced small cap fund managers in Australia. Michael was also one of the first managers of a boutique listed investment company, running the listed investment company Pacific Strategic Investments (PSI.ASX) which is now part of Brickworks Investment Company (BKI.ASX), an \$800m investment company.

While at Adam Smith Asset Management, a specialist small companies manager he jointly founded, he was awarded the IMCA/Money Management fund manager of the year award for small cap Australian equities.

Michael regularly appears on ABC radio, CNBC and the Australian Financial Review. Michael also writes for the Glennon Capital Weekly Newsletter.



INVESTMENT CREDENTIALS



Alex Shevelev
Portfolio Manager

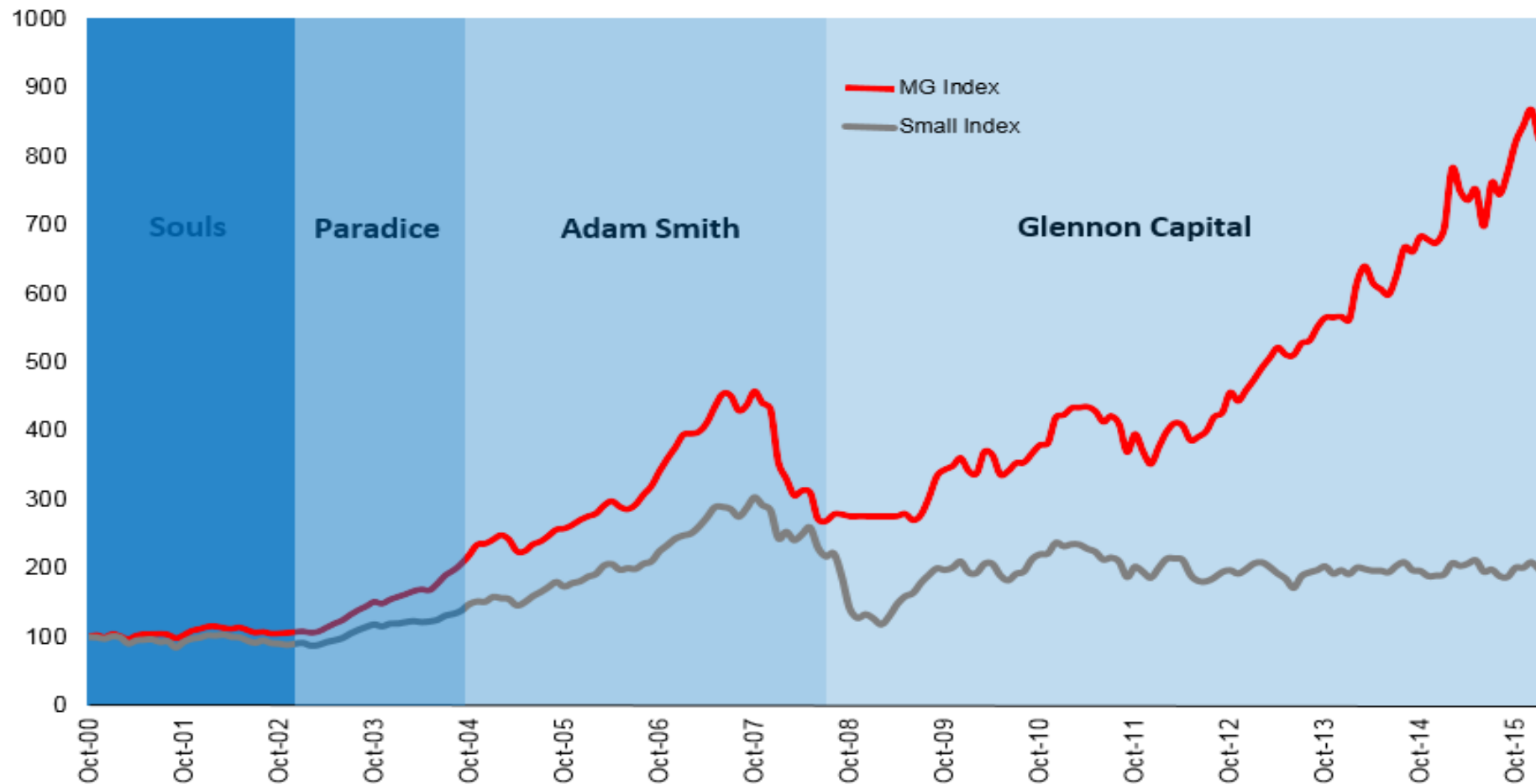
- 10+ years experience in financial markets
- 10+ years focused on small cap companies
- Analyst and portfolio manager roles at leading boutiques
- Previous roles at Cadence Capital, Atom Funds, Eight Investment Partners and Sky Funds Management
- Coverage has included domestic and global small cap equities with experience across industrials and resources

10 years experience in funds management as an analyst and portfolio manager with several leading boutique investment management firms. After starting his career at Cadence Capital researching small companies, Alex joined Eight Investment Partners with responsibility for coverage of domestic and regional small and large companies. Alex then founded Sky Funds Management to focus on domestic and international small companies.

Alex has had broad responsibility across Australian, regional and international small caps, as well as a wide range of sectors; including industrials and resources. Alex is a CFA charterholder and a CAIA charterholder. He also writes for the Glennon Capital Weekly Newsletter.



EXPERIENCE THROUGH CYCLES



The above represents a composite index of institutional portfolios. Performance from portfolio management at Republic from October 2000 to December 2002, Paradise from January 2003 until December 2003, and from ASAM from January 2004 until September 2008.

WHAT WE DO

INVESTMENT PROCESS



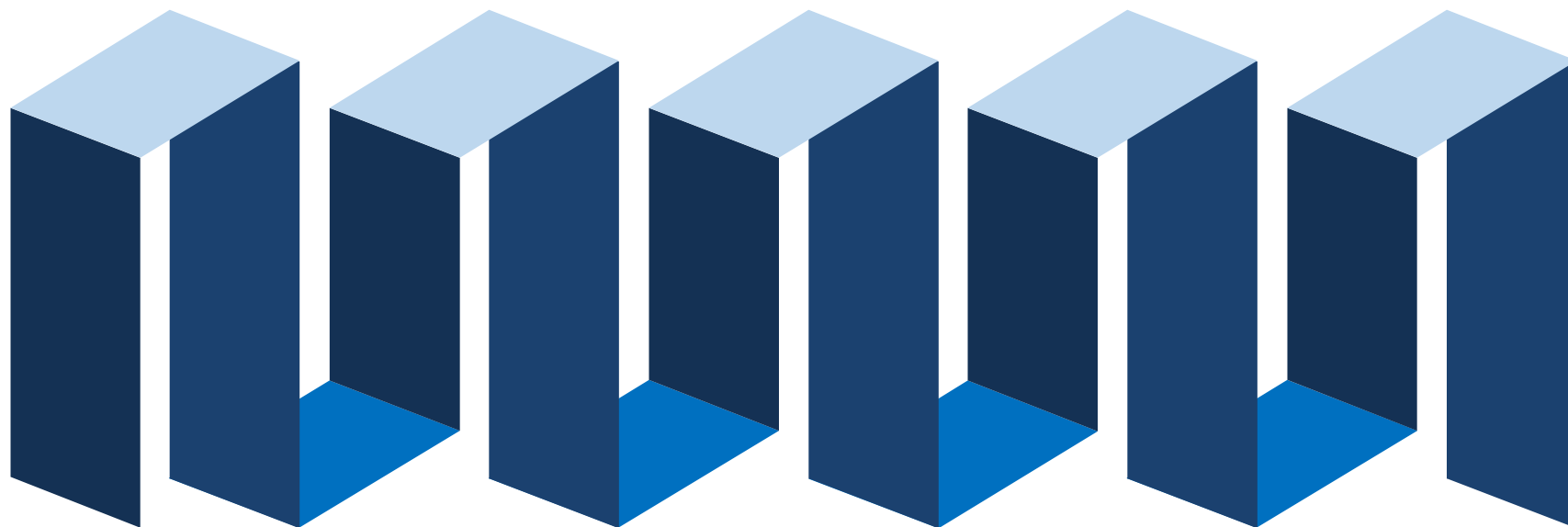
WHAT WE LOOK FOR

Superior management

- ✓ track record of success
- ✓ skin in the game

Growth prospects

- ✓ industry or market share
- ✓ revenue or margins



Sustainable businesses

- ✓ without excessive debt
- ✓ a history of profitability

Industry with barriers to entry

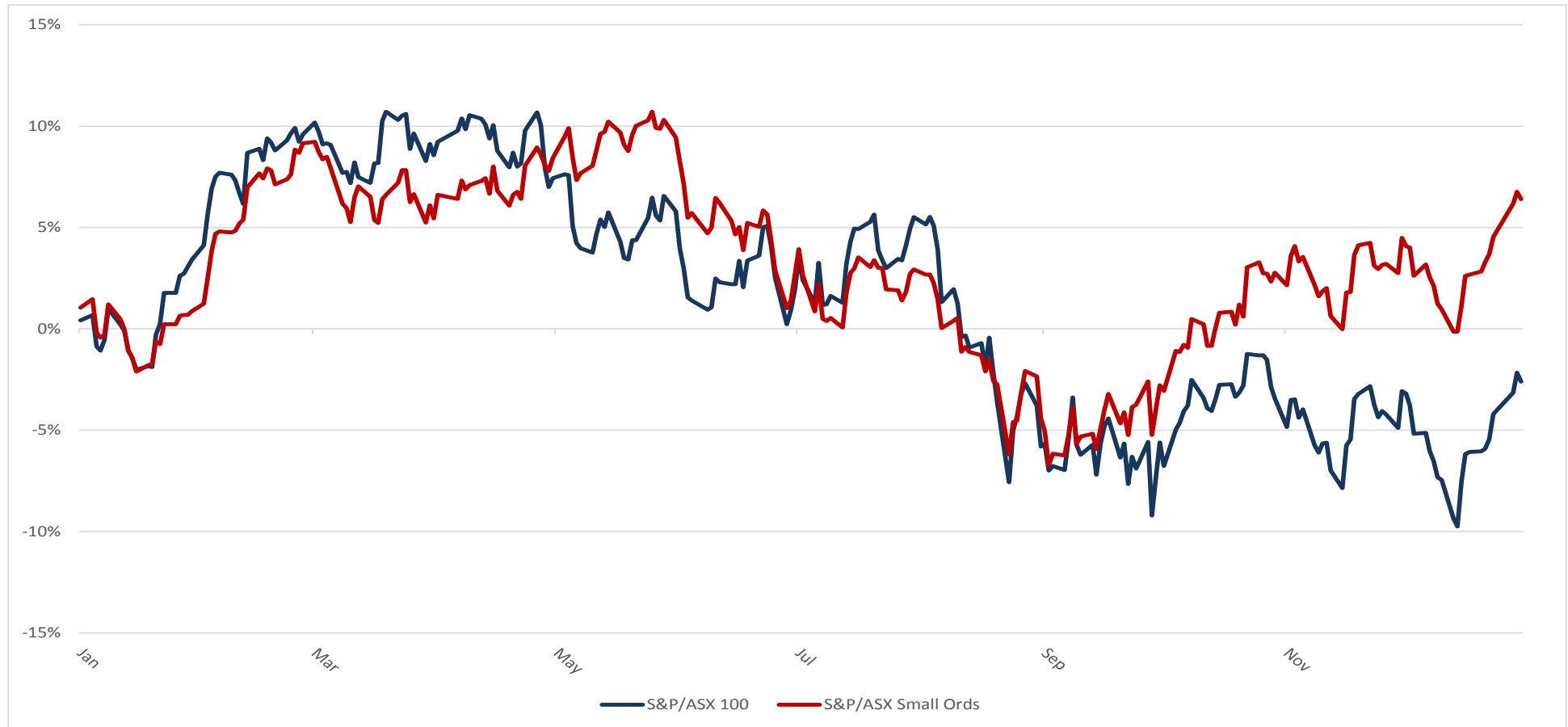
- ✓ reduces competition potential
- ✓ provides increased confidence

Undervalued

- ✓ flexible use of valuation metrics

MARKET OVERVIEW

THE AUSTRALIAN MARKET IN 2015



Small caps outperformed large caps in 2015

STOCK SELECTION IN SMALL CAPS

**BEST 10 STOCKS FROM
SMALL ORDINARIES**

+352%

**WORST 10 STOCKS FROM
SMALL ORDINARIES**

-72%

**SMALL ORDINARIES
INDEX RETURN**

6.4%

**BEST 10 STOCKS
FROM ASX 100**

+63%

**WORST 10 STOCKS
FROM ASX 100**

-42%

**ASX 100
INDEX RETURN**

-2.6%

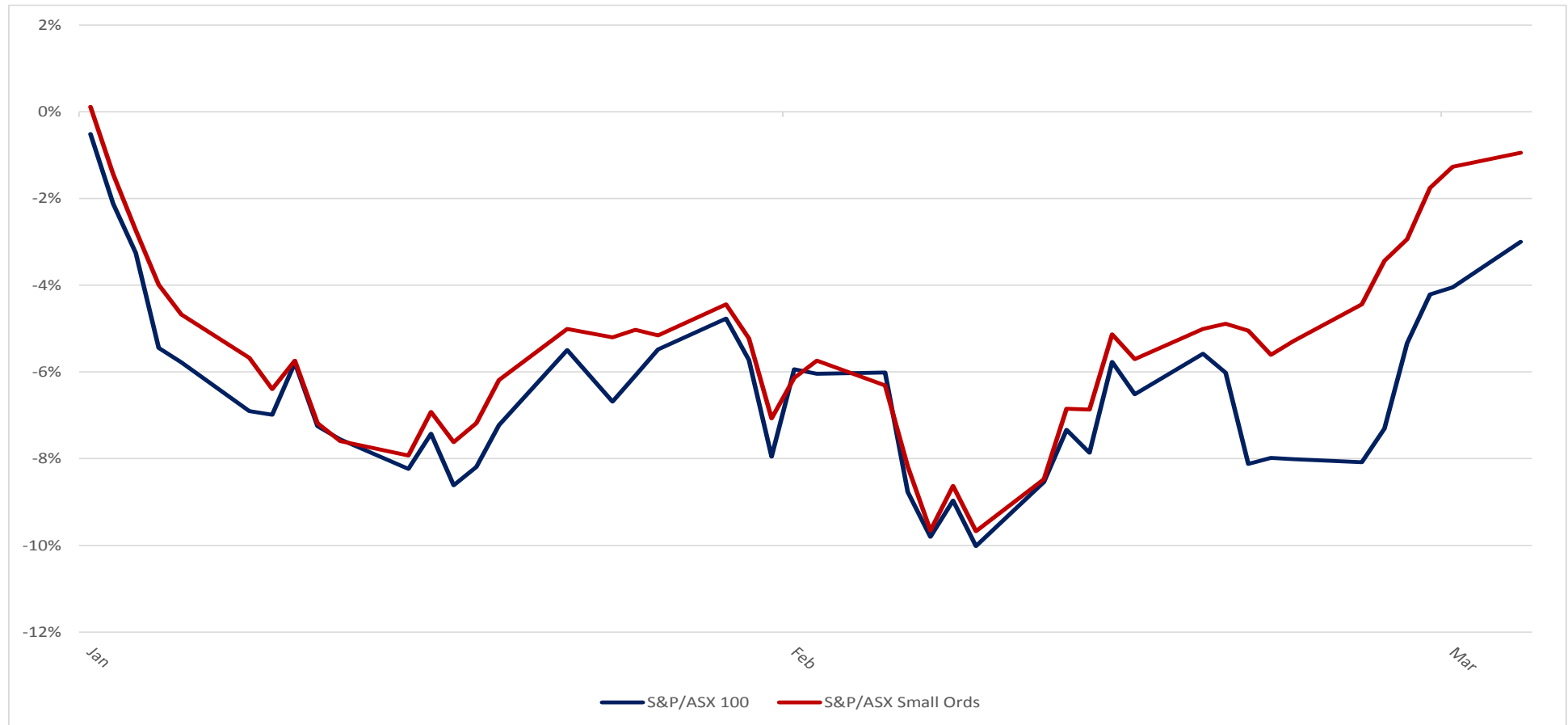
Best small caps outperform worst by 424% in 2015; in large caps only 105%



SMALL CAPS IN 2015

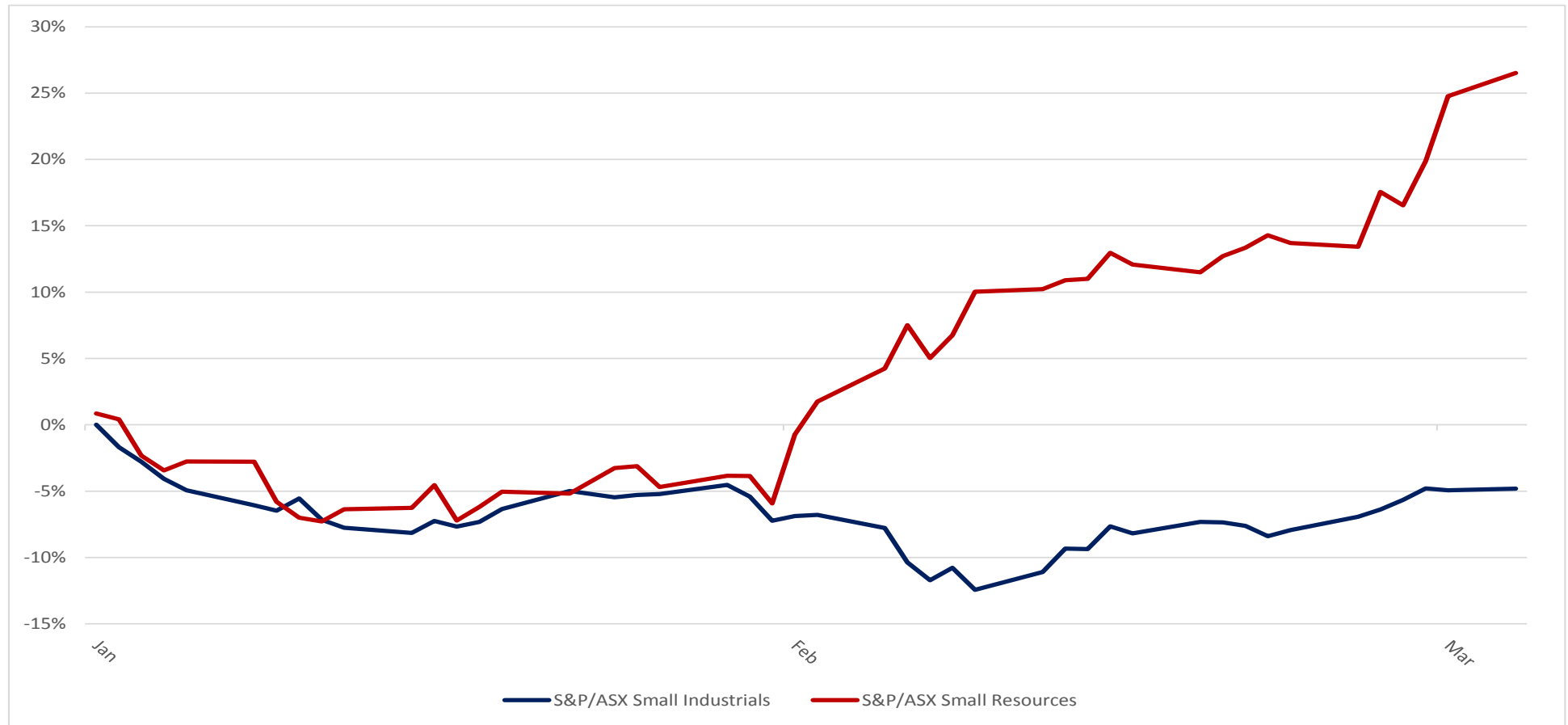
- Active management in small caps is critical
- There were many disasters
 - Slater & Gordon
 - Arrium
 - Energy sector
- But also many opportunities to deliver returns
 - Outdoor advertising
 - Blackmores and Bellamy's
 - Selected gold stocks
- Some drivers are set to continue into 2016
 - Others may continue but are already priced into stocks
 - While others may cease or reverse
- Provides opportunity to outperform

THE AUSTRALIAN MARKET IN 2016



Small caps outperformed large caps so far in 2016

SMALL CAPS IN 2016

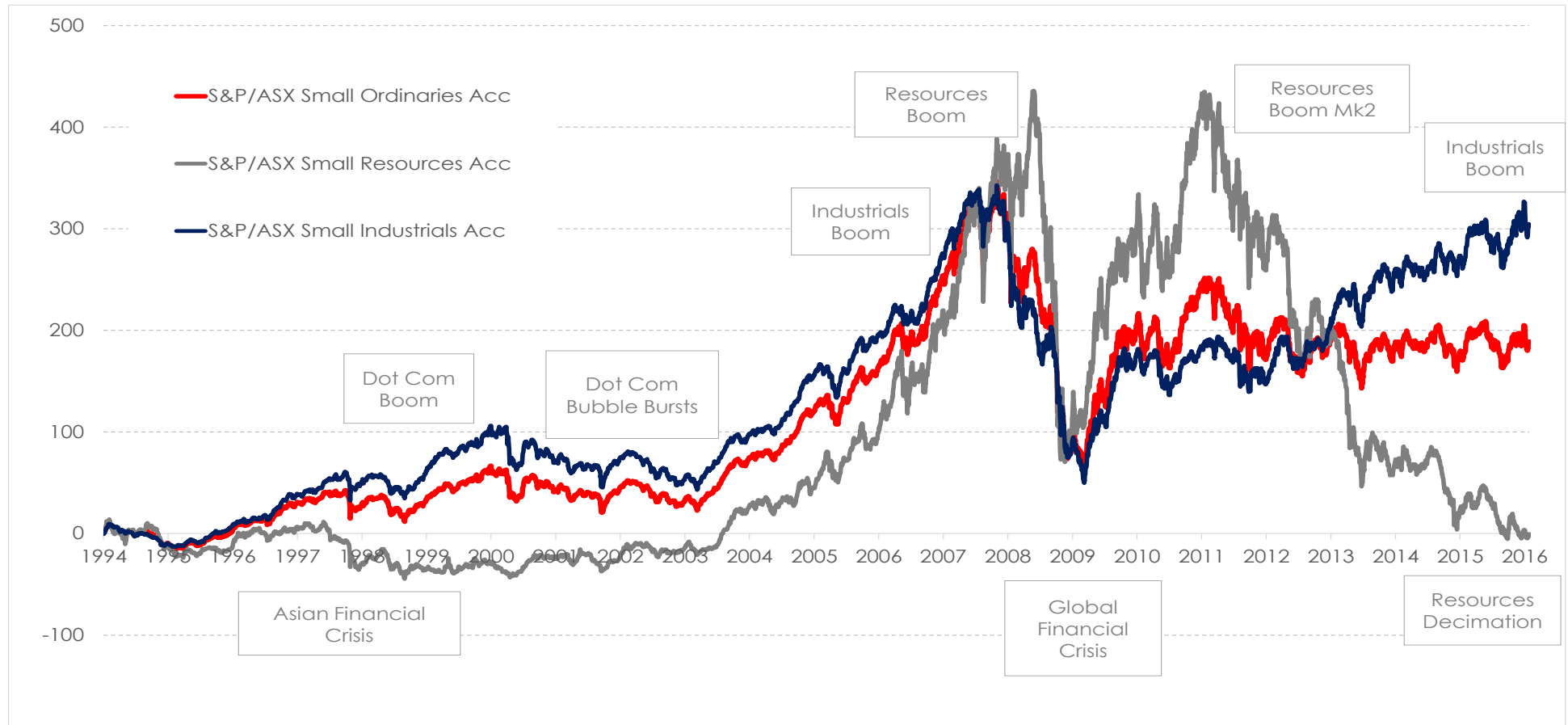


Small resources substantially outperforming small industrials so far in 2016

SMALL CAP BOOMS AND BUSTS

- Active management in small caps is critical
- Resources as a proportion of the small cap index was
 - 12% in 2002
 - 46% in 2011
 - 12% in 2015
- Keeping an eye out for bubbles; investors buying stocks at
 - cyclically high revenues
 - unsustainably high margins
 - peak multiples
- Revenue multiples made a comeback in 2015

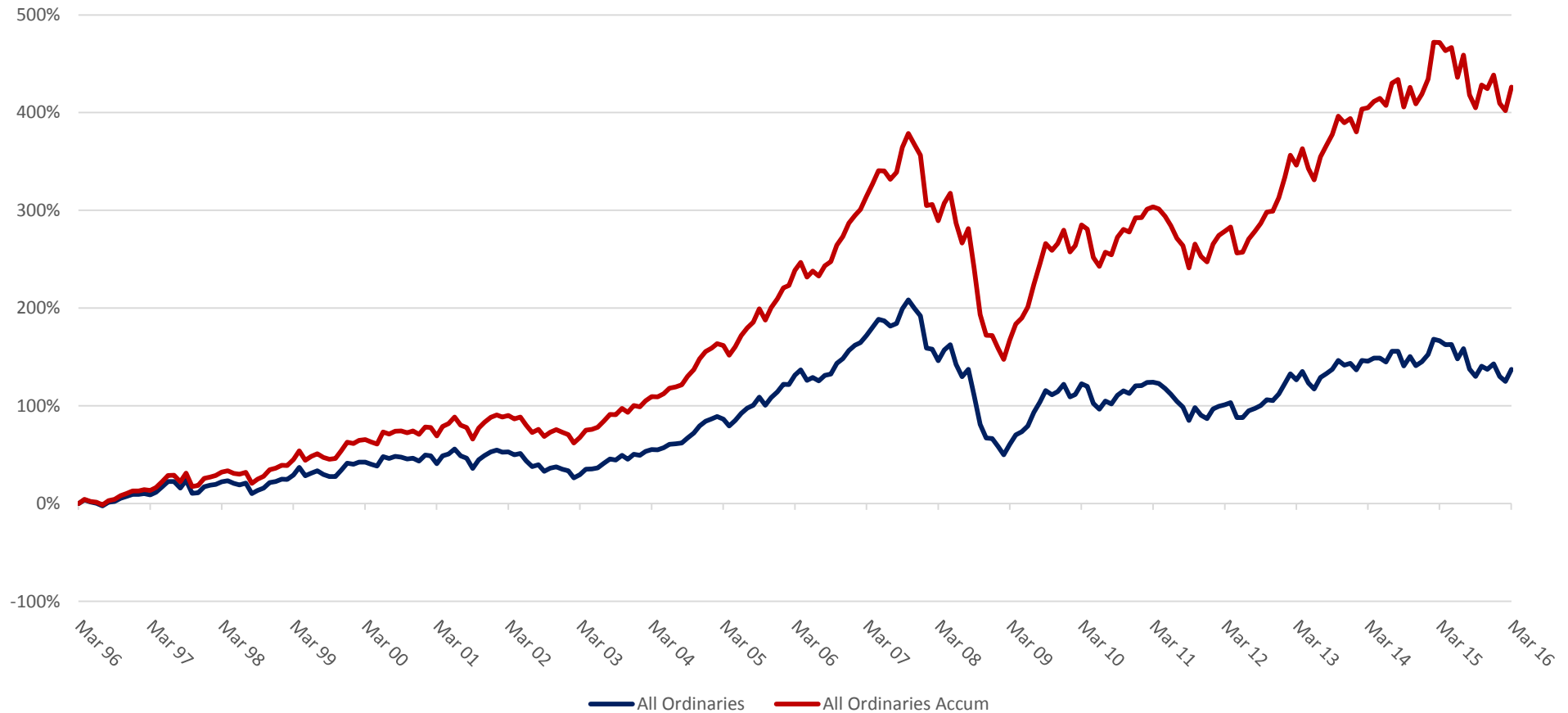
SMALL CAPS CHANGE SIGNIFICANTLY OVER TIME



Booms and busts come and go

DIVIDENDS

LONG TERM DIVIDENDS ARE IMPORTANT



Reinvesting dividends yields substantially better results over the long term

DIVIDENDS

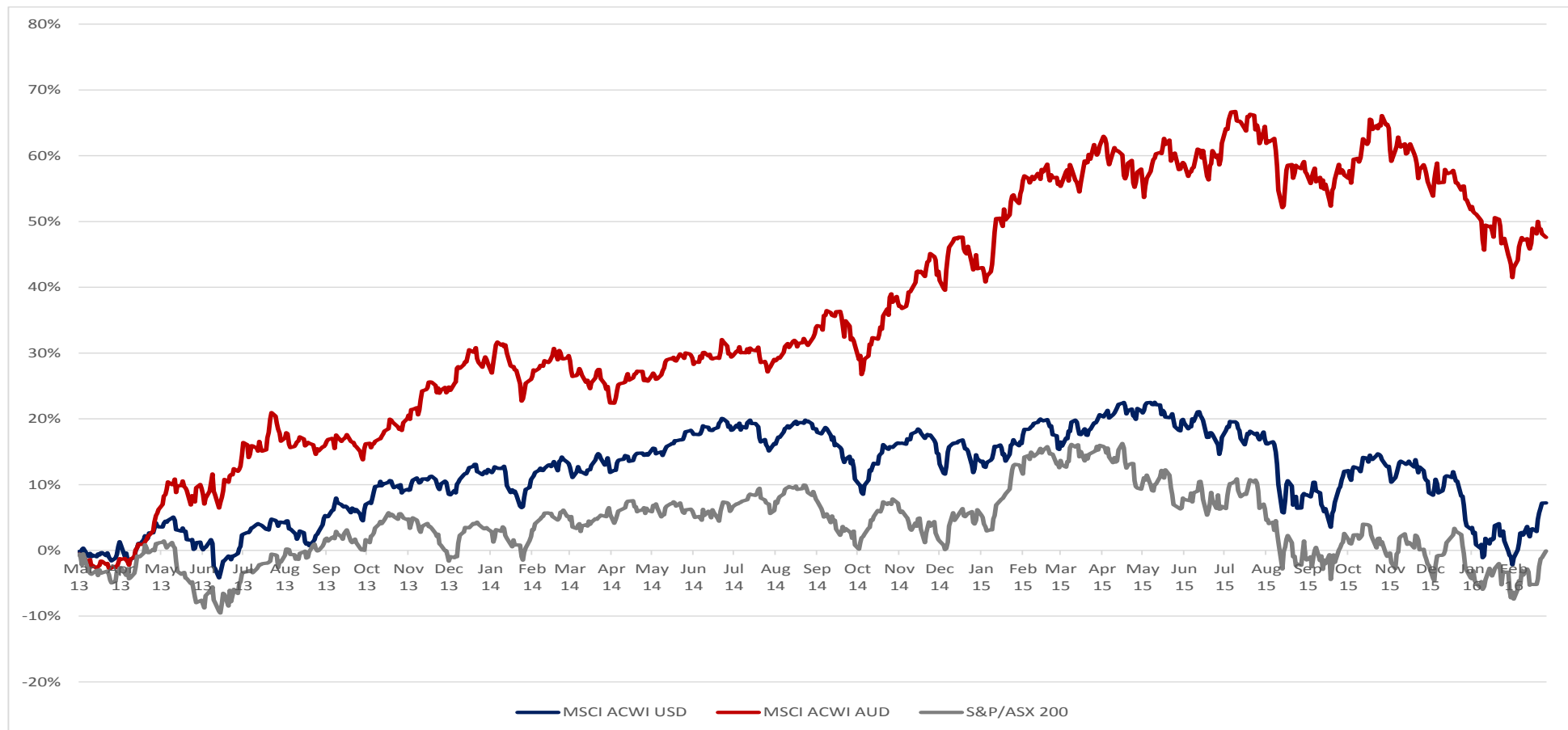
- Reinvesting dividends allows capital to compound
- This is true for listed investment companies also
- GC1 has a dividend reinvestment plan (DRP) in place
- The GC1 DRP allows investors to reinvest dividends at a discount to the prevailing market price
- Under the DRP investors
 - pay no brokerage
 - still receive imputation credits
 - may participate for all or part of their holding

THE OFFSHORE TREND



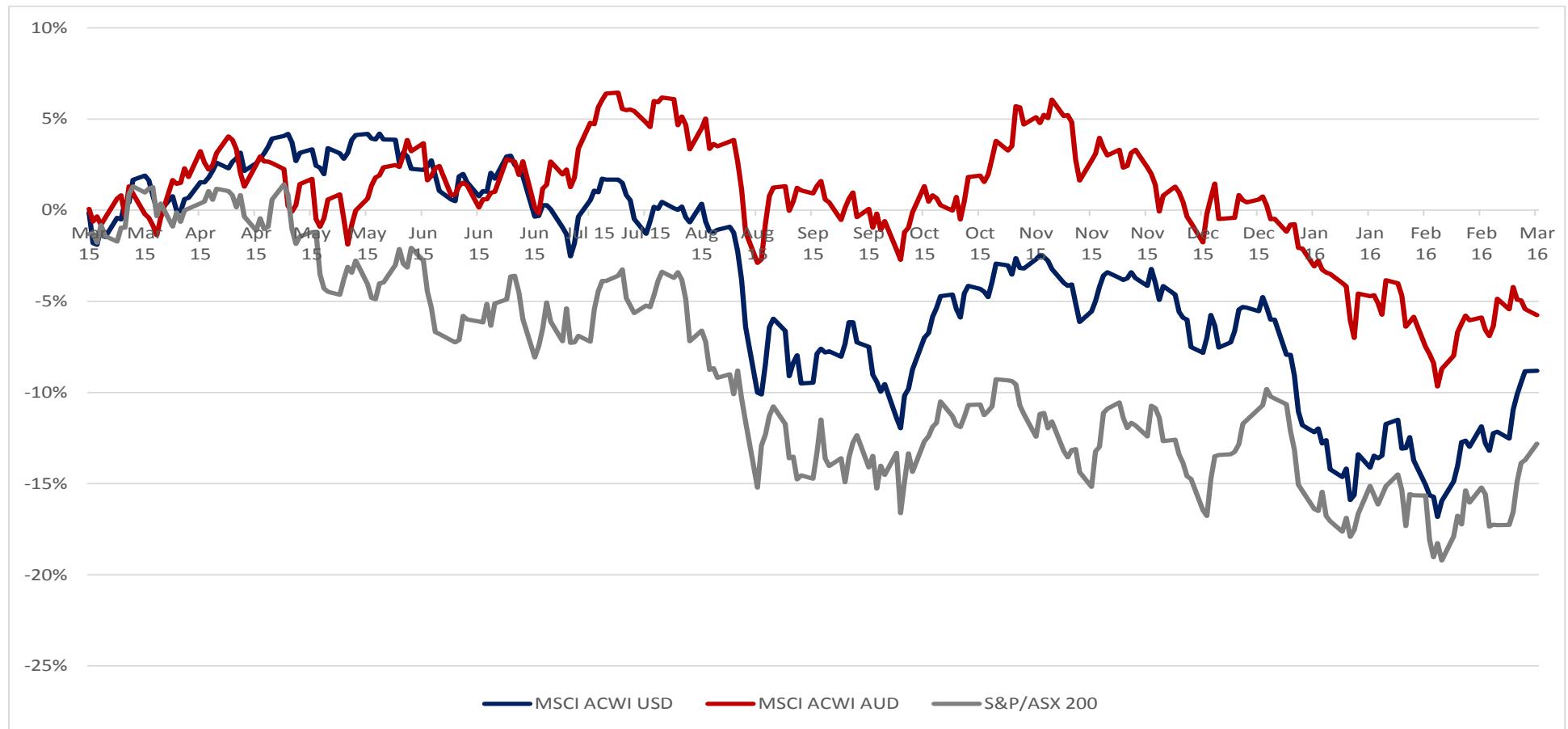
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INTERNATIONAL MARKET RETURNS



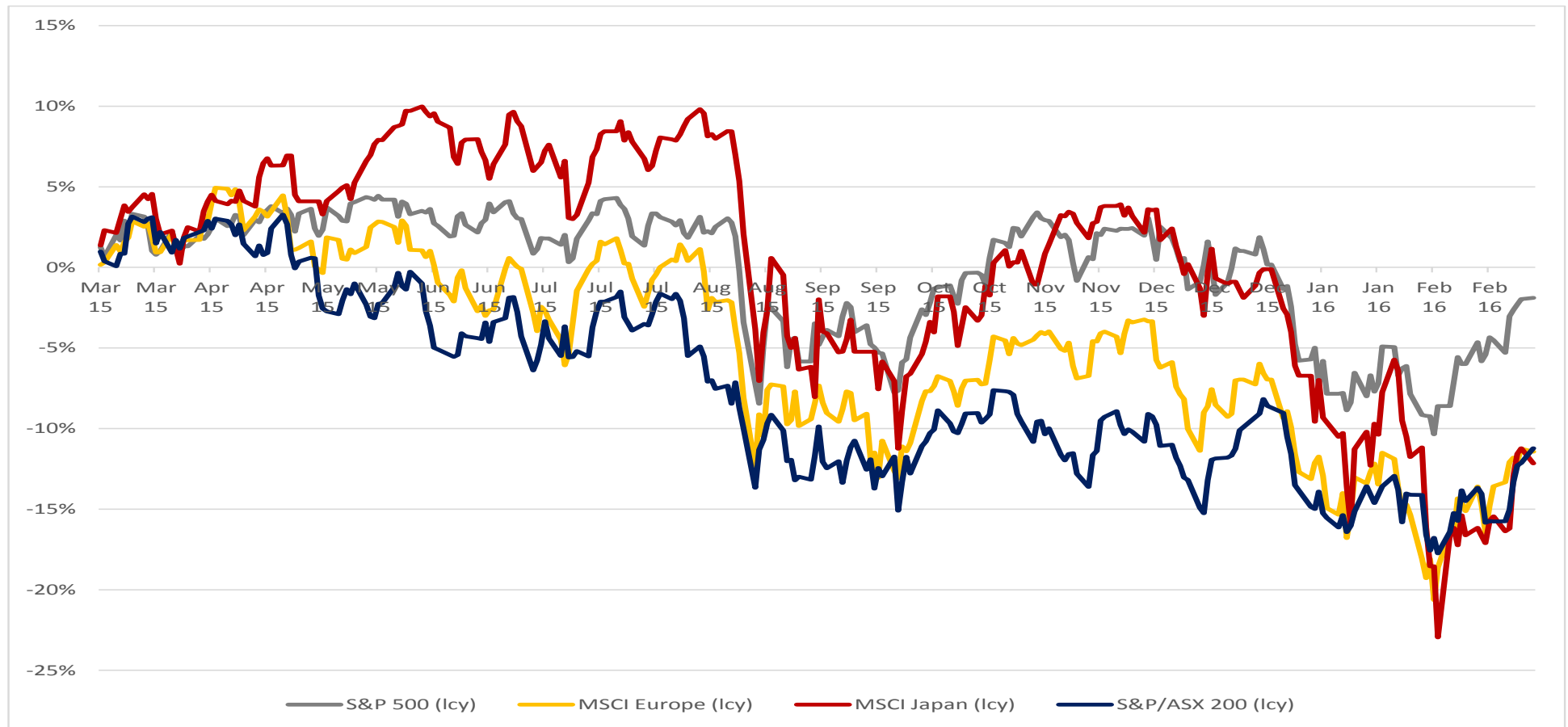
Local currency returns for international markets and domestic have been similar

INTERNATIONAL MARKET RETURNS



Local currency returns for international markets and domestic have been similar

INTERNATIONAL MARKET RETURNS



Over the past year most markets have performed poorly in local currency

OFFSHORE IMPACT

- Over the past 3 years the Australian dollar has fallen from a high of \$1.05 to 75c. This has been a significant benefit to holders of equities with non-AUD earnings
 - Listed in Australia
 - Listed overseas
- The impact of this benefit has stalled
- Some currency benefits are structural
 - a lower cost base for an export businesses
- Some currency benefits are one-off
 - timing differences
- Glennon Capital has held Australian listed stocks with international earnings
 - Sirtex
 - IPH
 - Mayne Pharma

INTEREST RATES, DIVIDENDS, YIELD

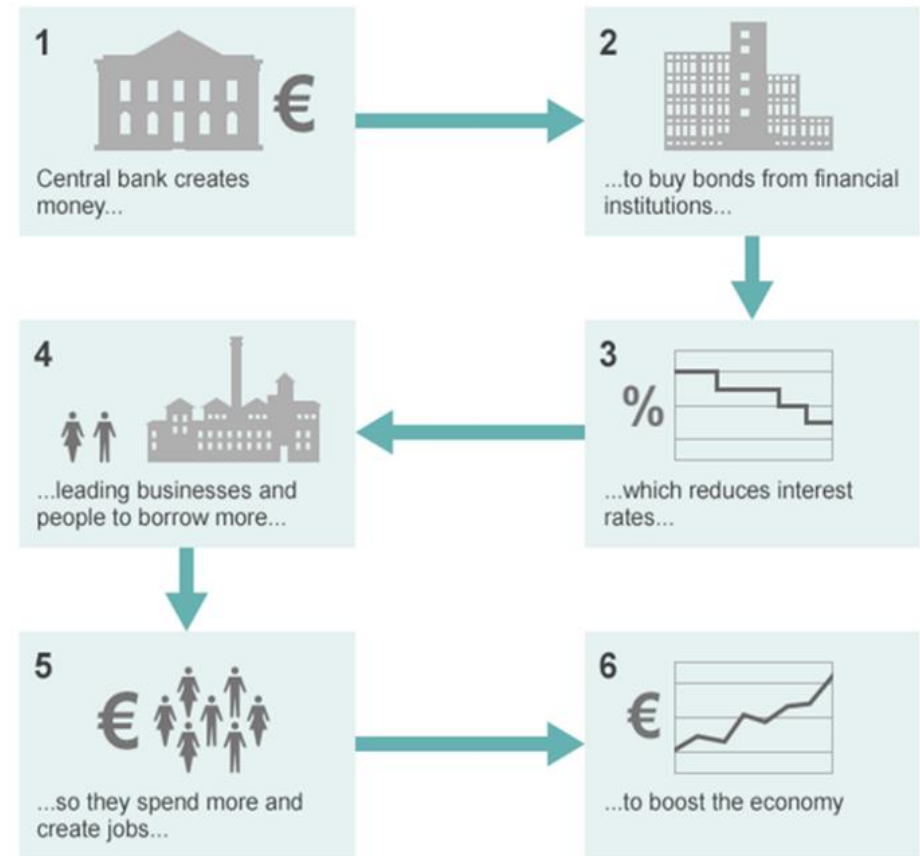


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GLOBAL ECONOMICS

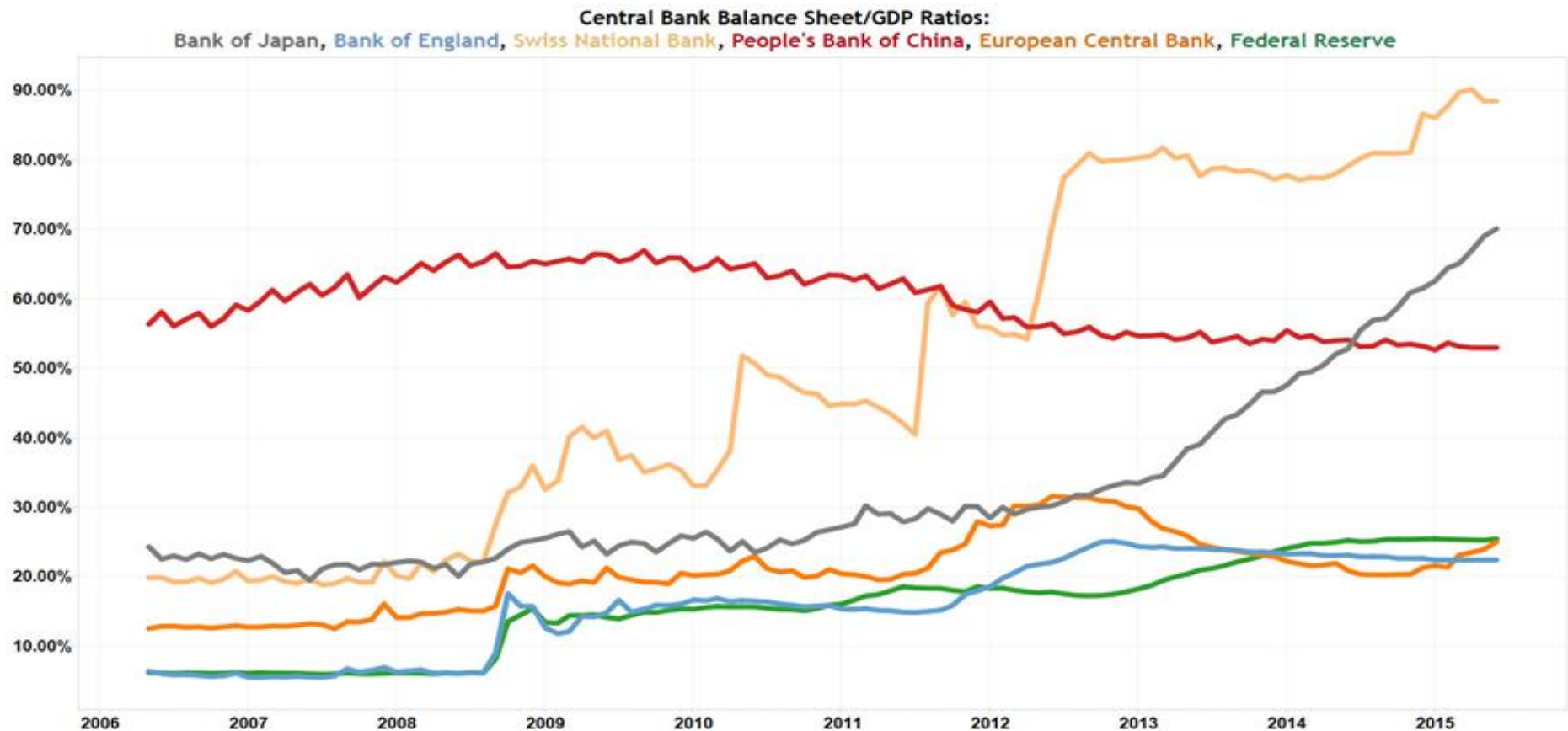
- Low interest rates globally
- Asset price bubbles form when interest rates are low
- Central banks are still buying bonds post the GFC
- However, the rate of buying has slowed
 - The US is no longer buying
 - China is selling
- Selling increases interest rates and slows growth
- Interest rates will eventually increase

Quantitative Easing: The theory



Source: BBC

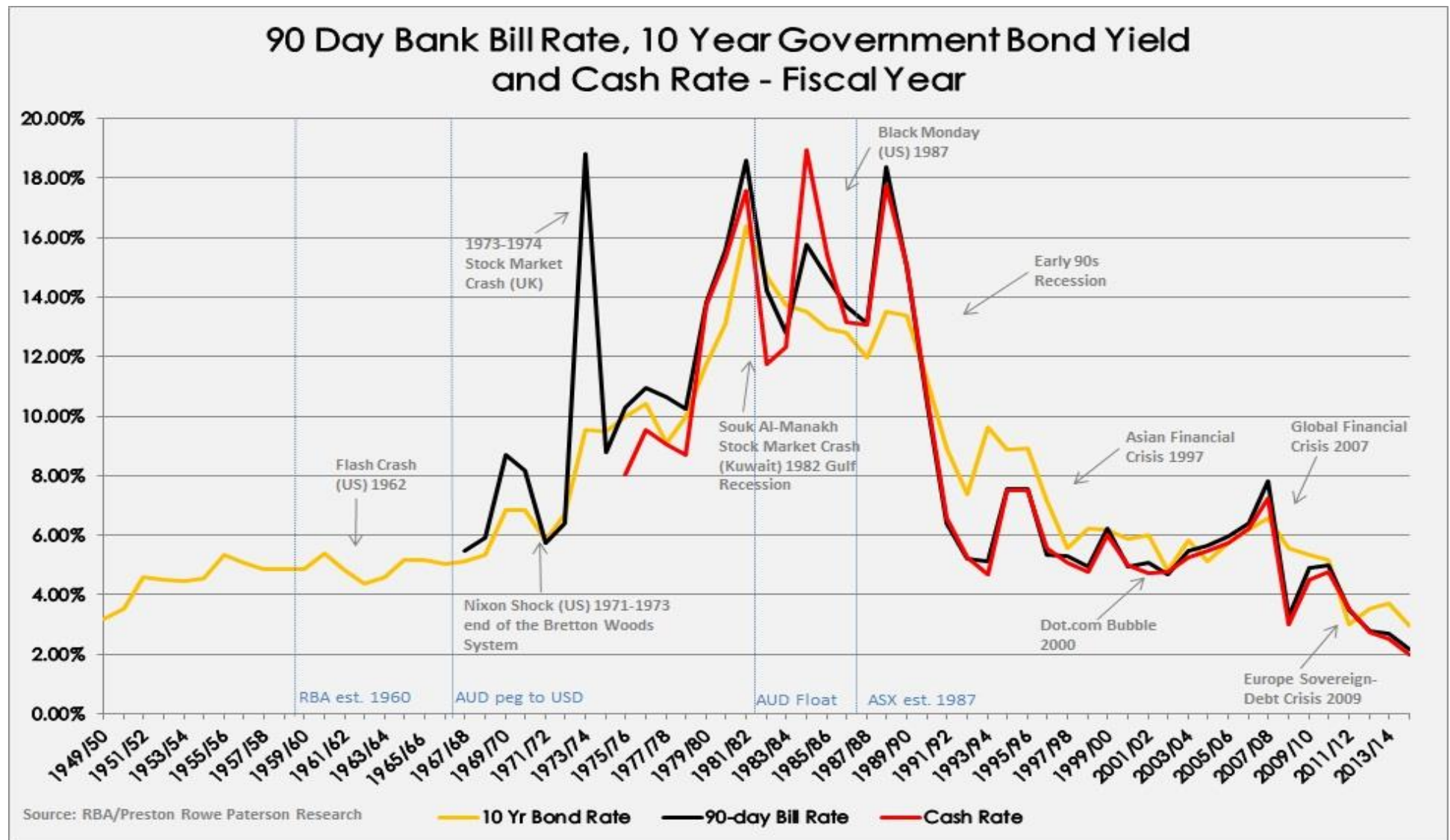
WHY ARE INTEREST RATES LOW?



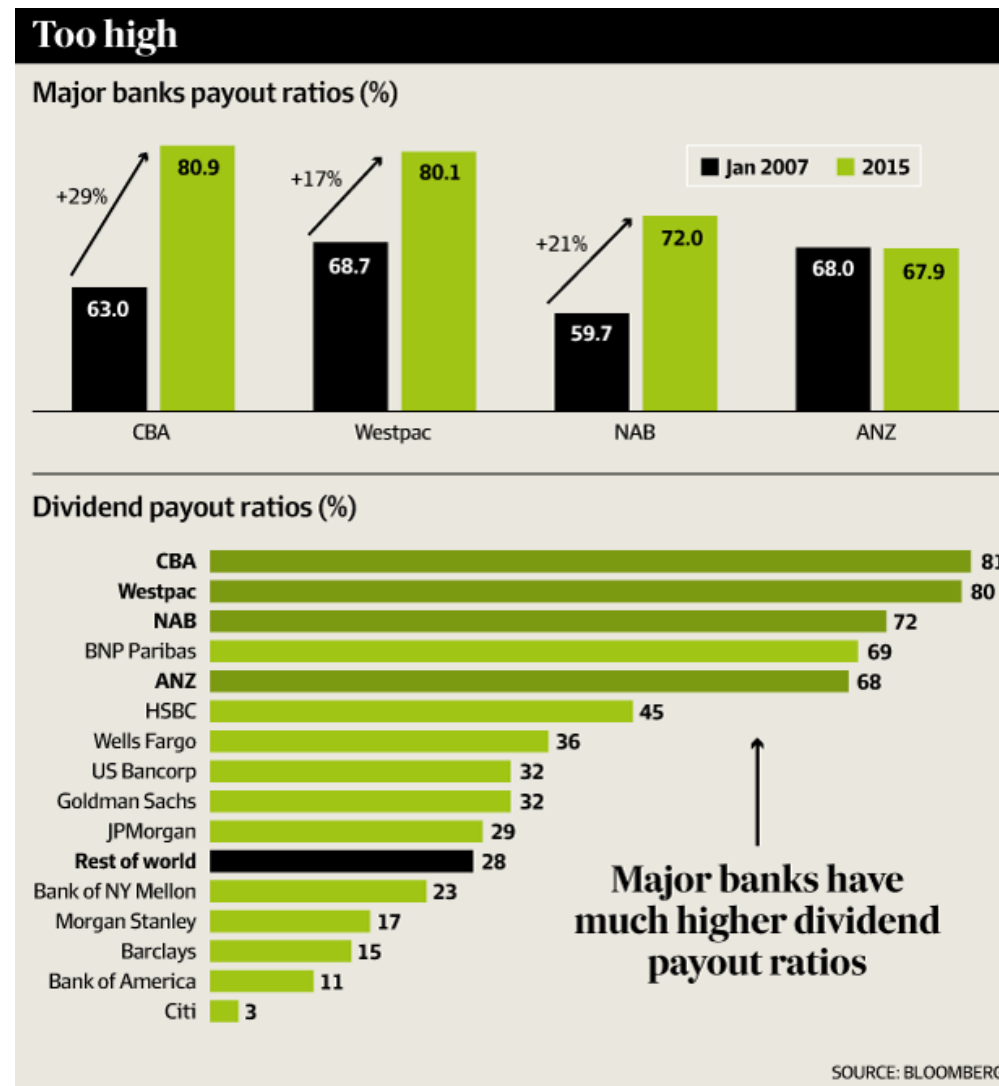
Source: Riskelia

Massive expansion of Central bank balance sheets

THE IMPLICATION FOR AUSTRALIA



AUSTRALIAN BANKS NOT REINVESTING



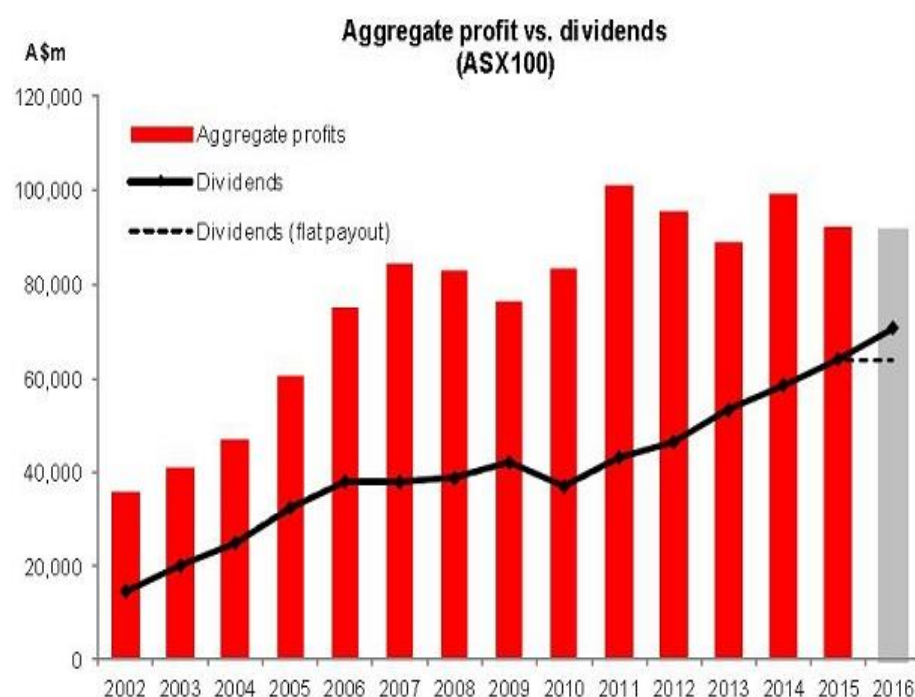
ASX 100 PAYOUT RATIO

Fig 12 Payout ratio for the ASX100 reaches all time high...



Source: Factset, Macquarie Research, January 2016

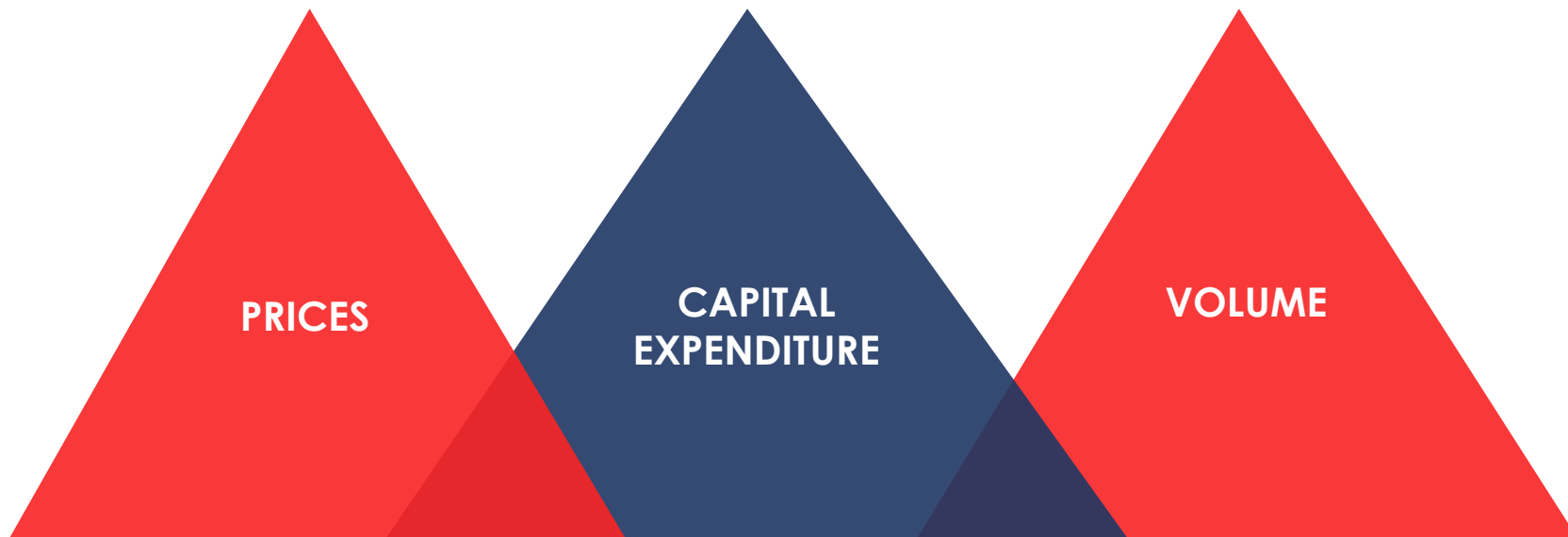
Fig 13 A flat payout ratio equates into a 10% decline in dividends paid...



Source: Factset, Macquarie Research, January 2016

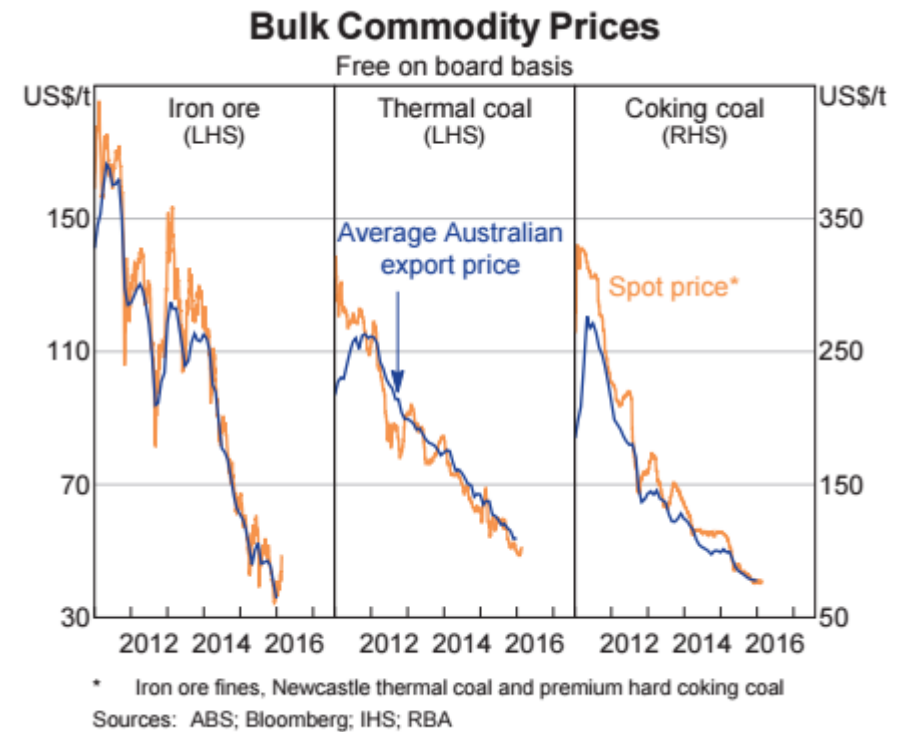
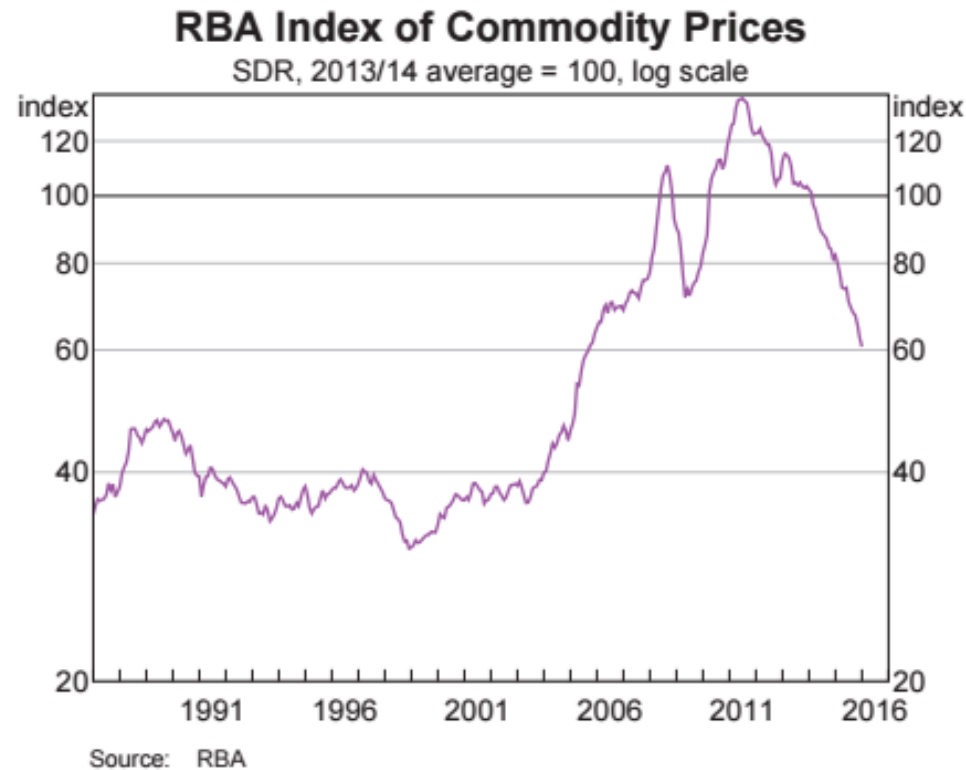
RESOURCES

THE BOOM IN PARTS



The resource boom was actually multiple booms

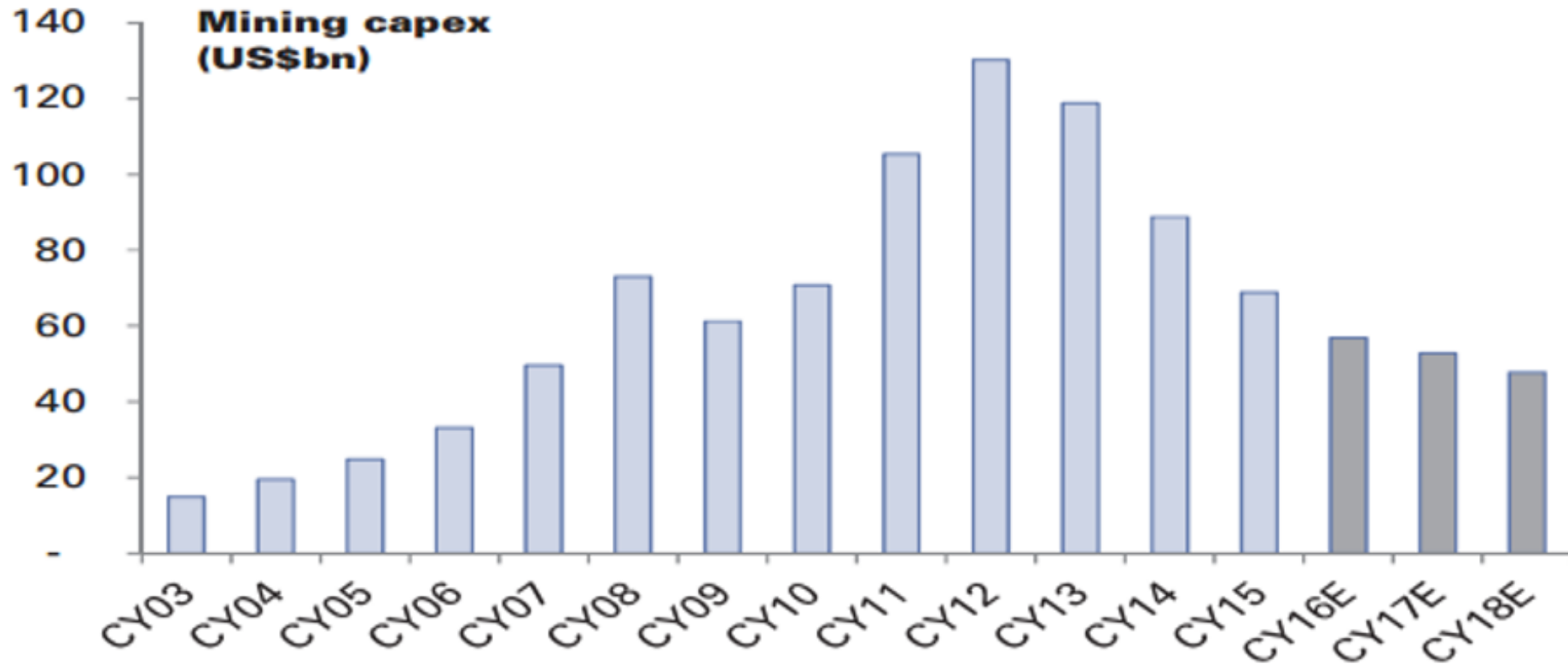
PRICES



Prices have fallen substantially



CAPITAL EXPENDITURE

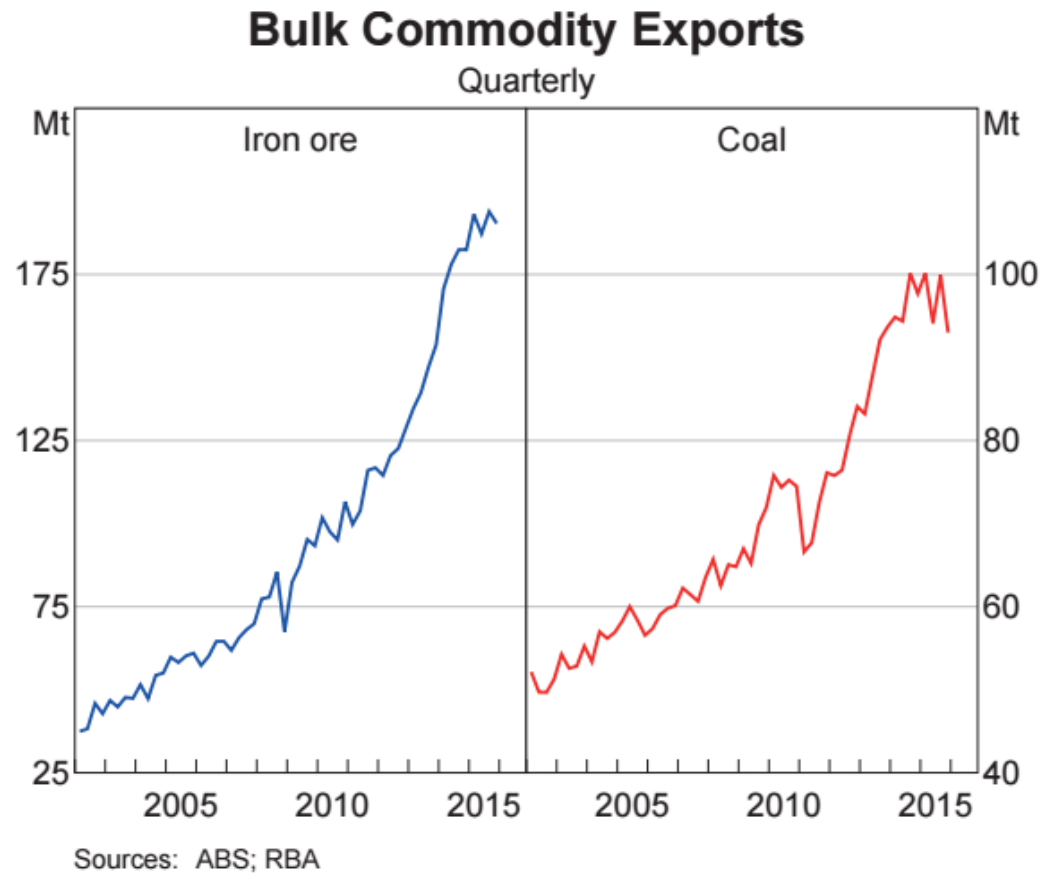


Source: Goldman Sachs

Capital expenditures have also fallen substantially

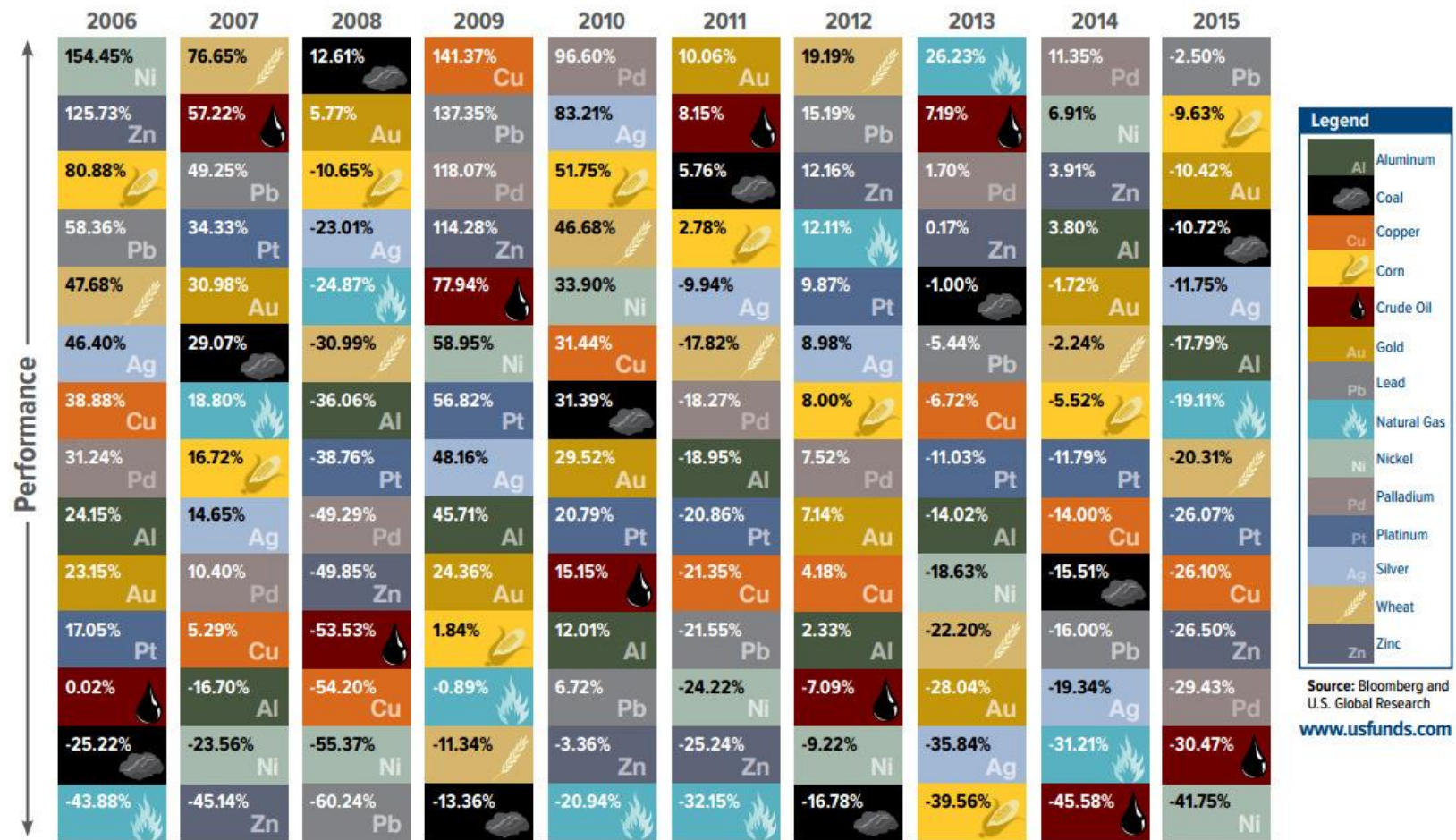


VOLUMES



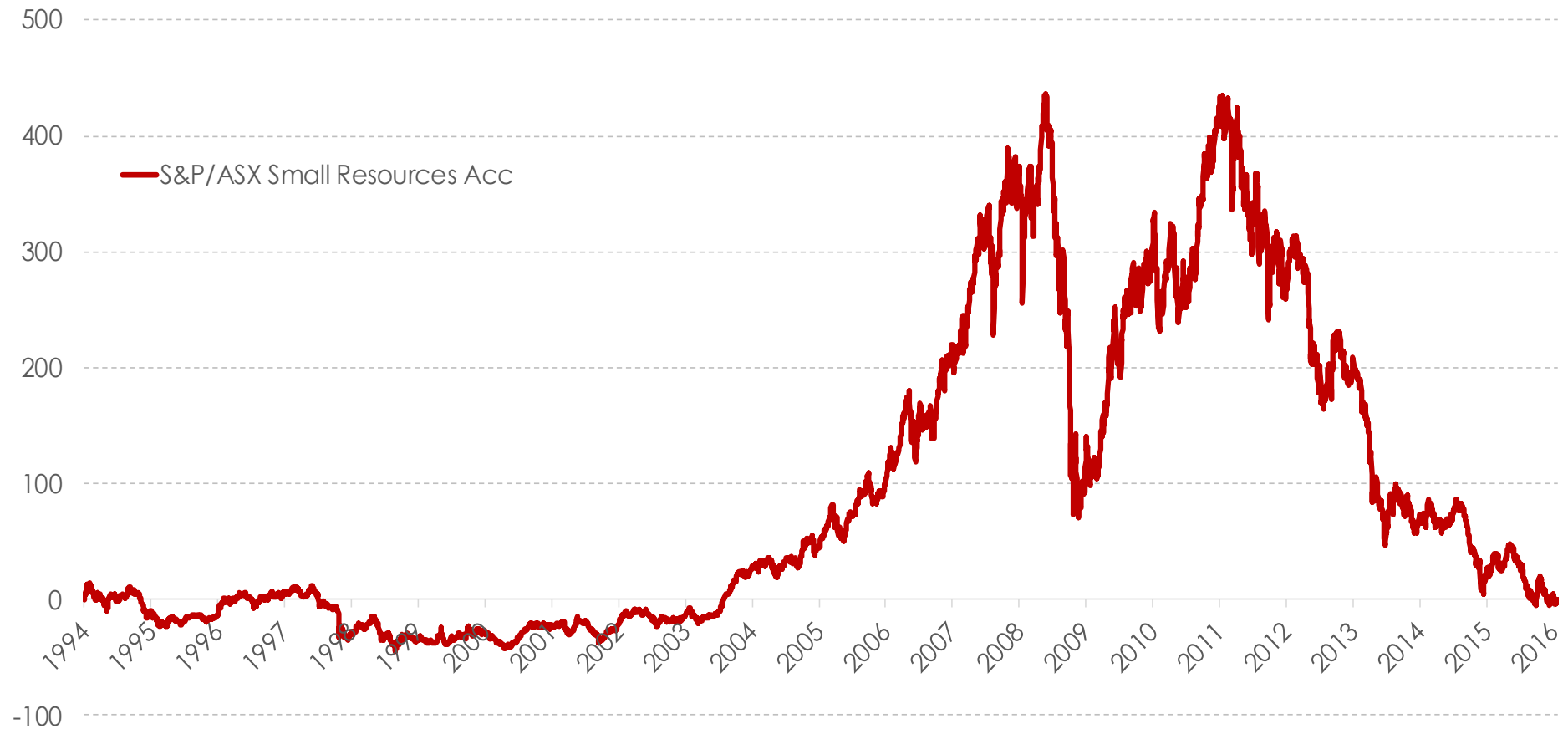
Volumes have continued to increase as supply increases

RESOURCES ARE NOT ALL THE SAME



Vast array of resources provide different returns;
though 2015 a poor year in USD terms

SMALL CAP RESOURCES



Small resources back to levels last seen in 2003

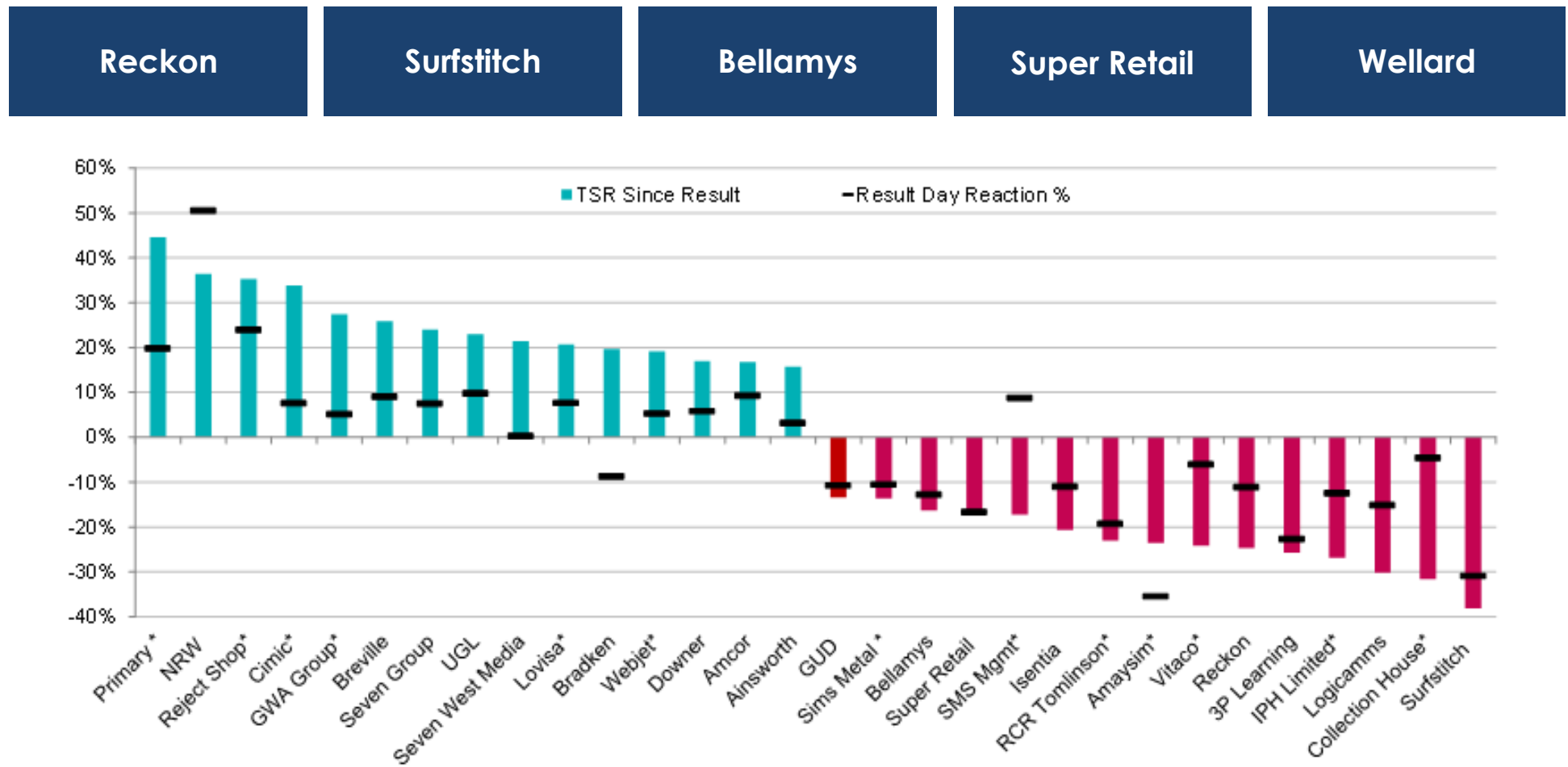
SOME BRIGHT SPOTS

- Small cap resources are down to levels last seen in 2003
- Some sign of supply side constraint; eg. Oil
- Company cost bases are different
 - a gold producer in Australia has benefitted from selling gold in US dollars, while paying Australian dollar mining costs
- Some mining services businesses have stabilised
 - Especially those aligned to volume of production and to gold
 - Capital expenditure has dramatically reduced, improving free cashflow
- Investors still shunning both mining and mining services
- Glennon Capital has recently taken small positions in gold and oil/gas exposed companies

REPORTING SEASON OVERVIEW

OBSERVATIONS FROM REPORTING SEASON

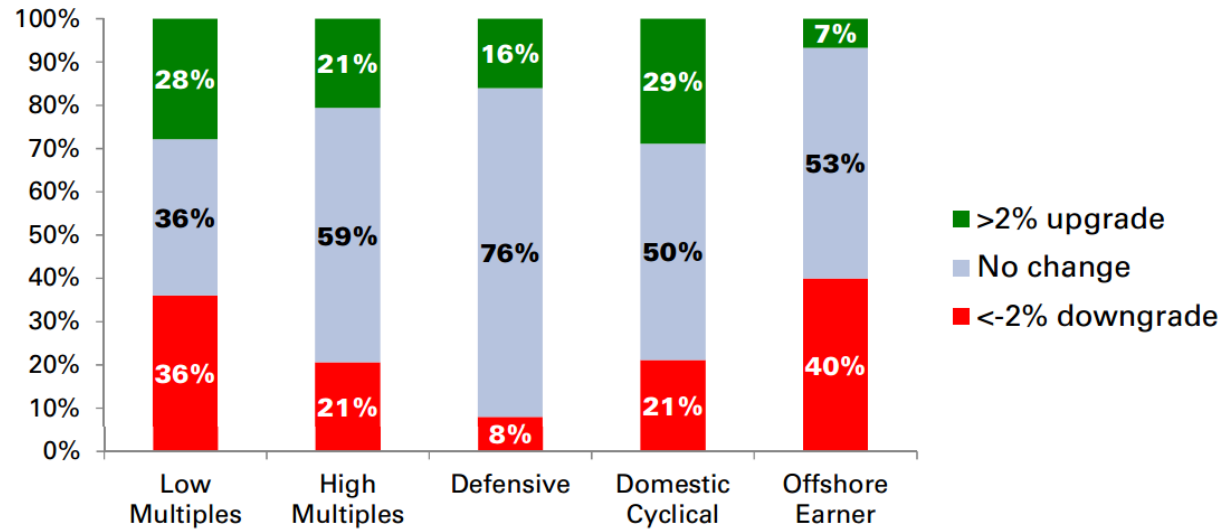
- The market is hyper sensitive to small earnings misses. There have been some over-reactions on the downside



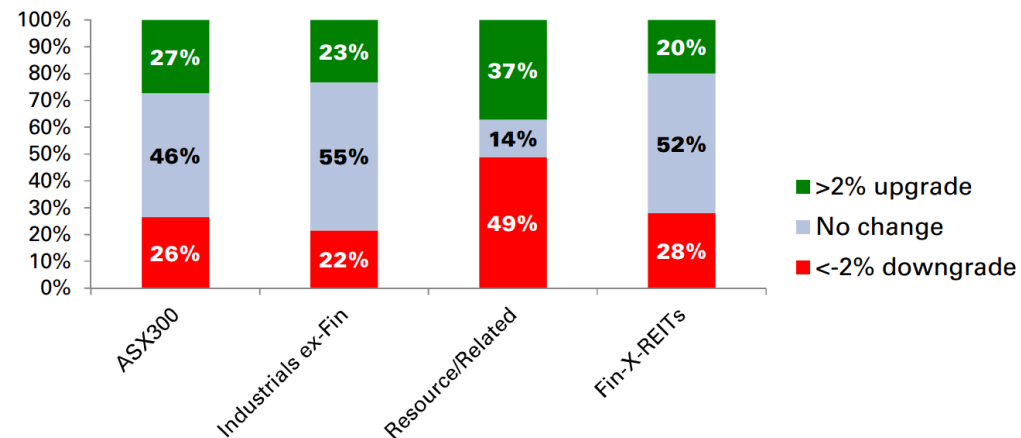
Source: Morgans

OBSERVATIONS FROM REPORTING SEASON

Distribution of FY16 Consensus EPS Revisions



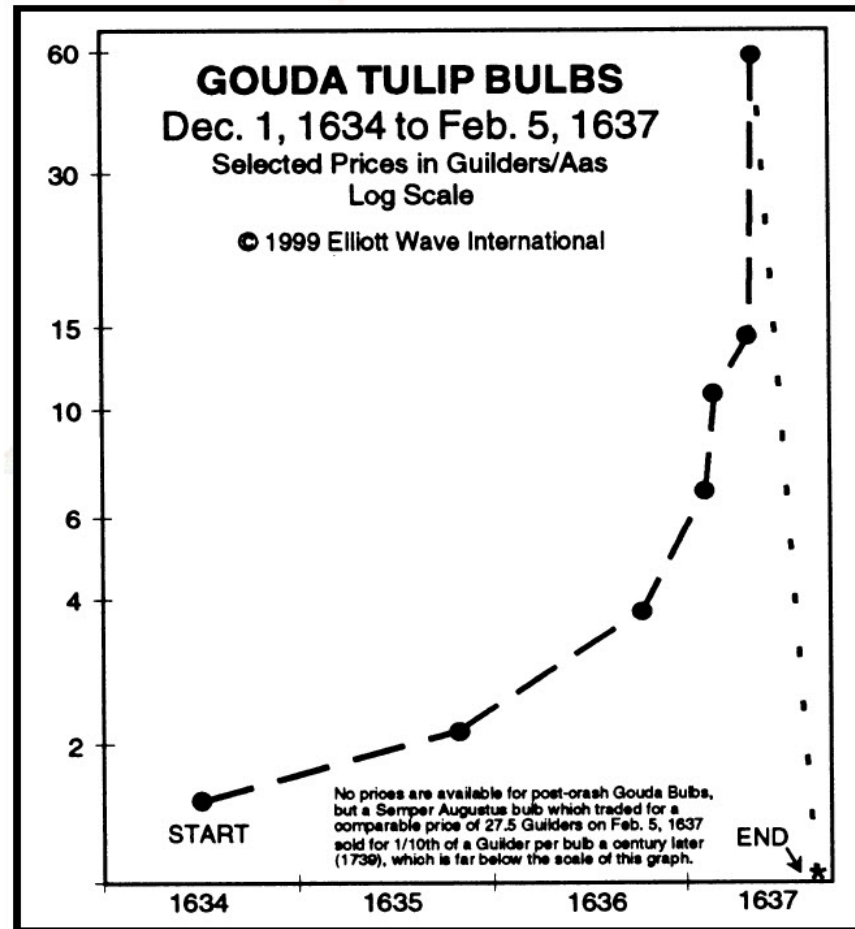
Distribution of FY16 Consensus EPS Revisions



Source: Goldman Sachs

BOOMS & CYCLES

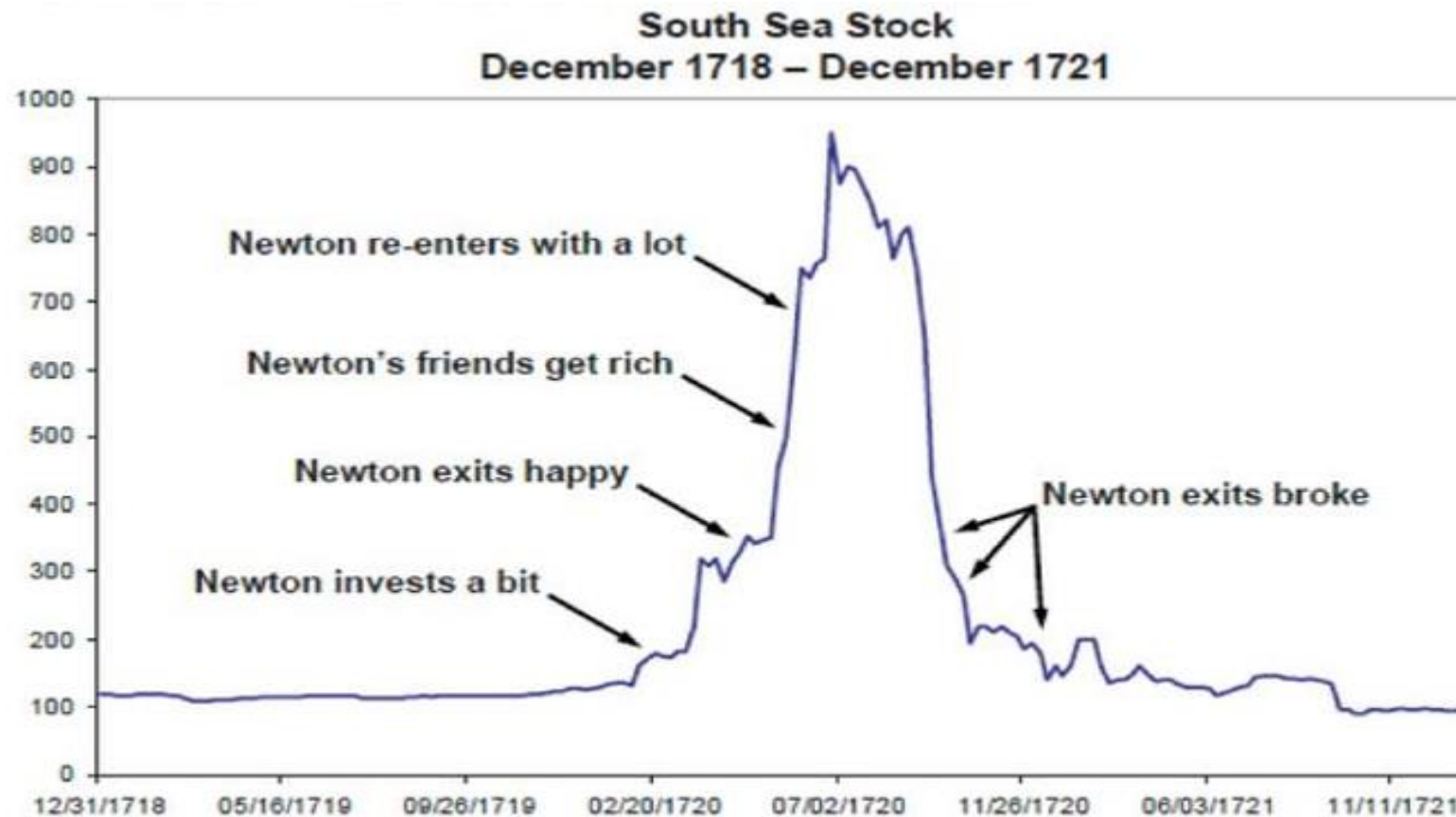
TULIPS



Booms and busts have been around for a long time



SOUTH SEA BUBBLE



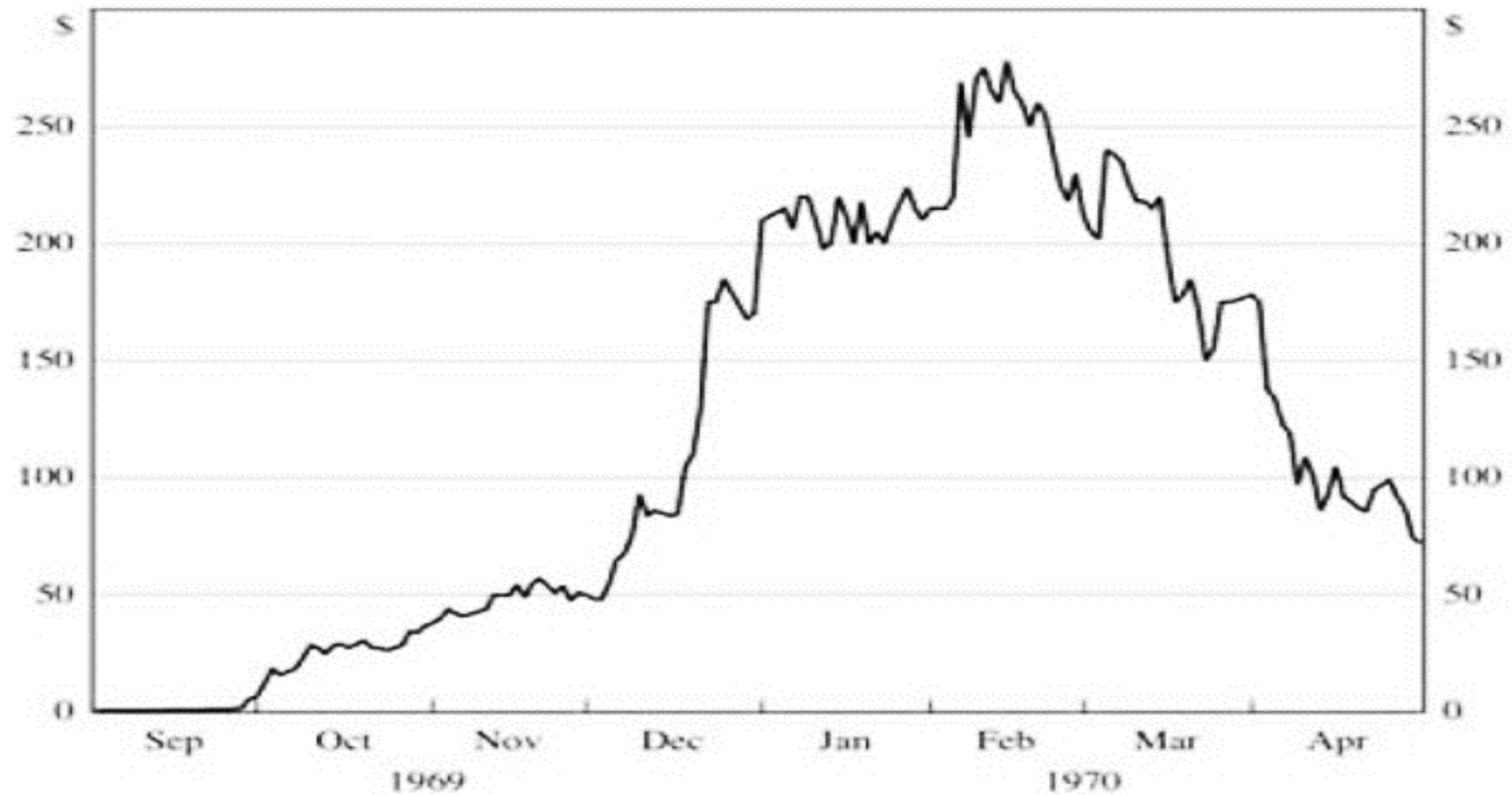
Marc Faber, Editor and Publisher of "The Gloom, Boom & Doom Report."

Booms and busts have been around for a long time



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POSEIDON NICKEL

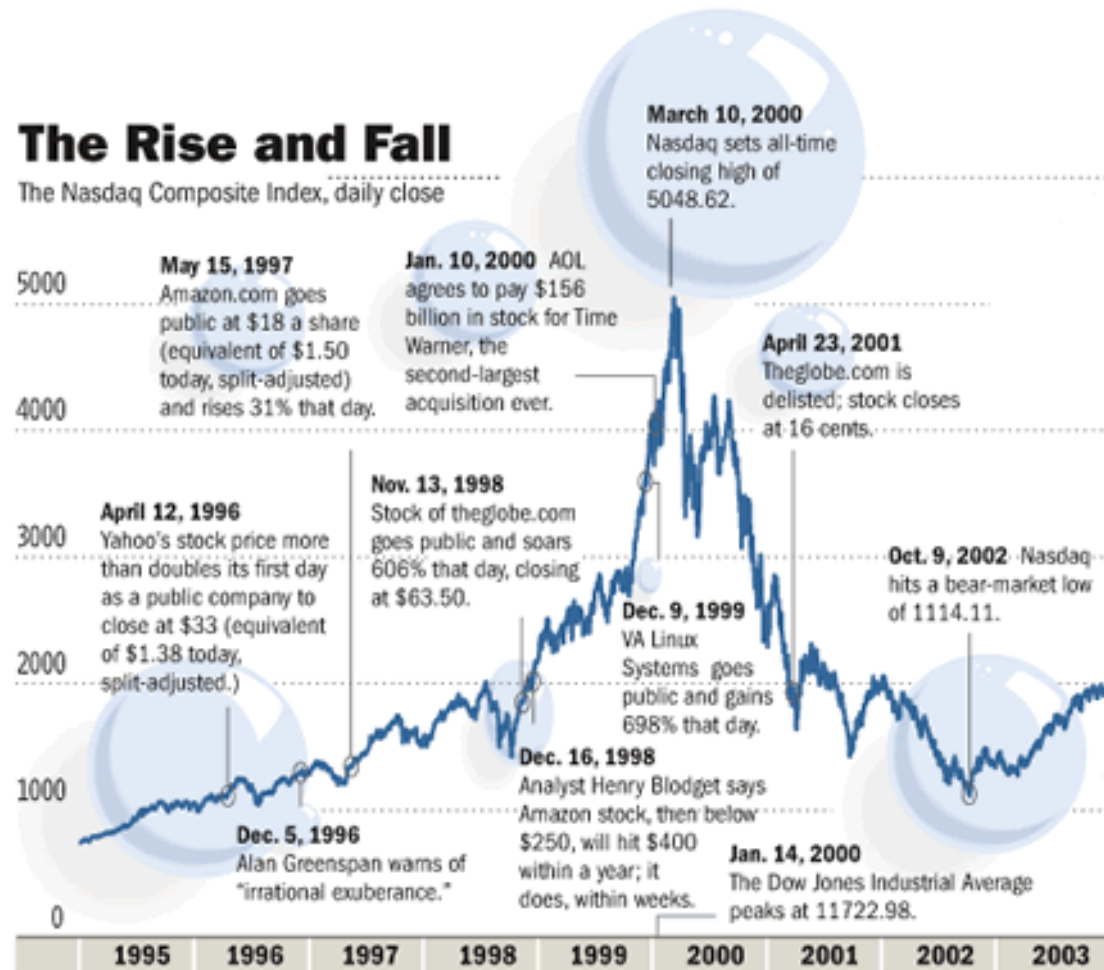


Five months of euphoria



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DOT COM BUBBLE



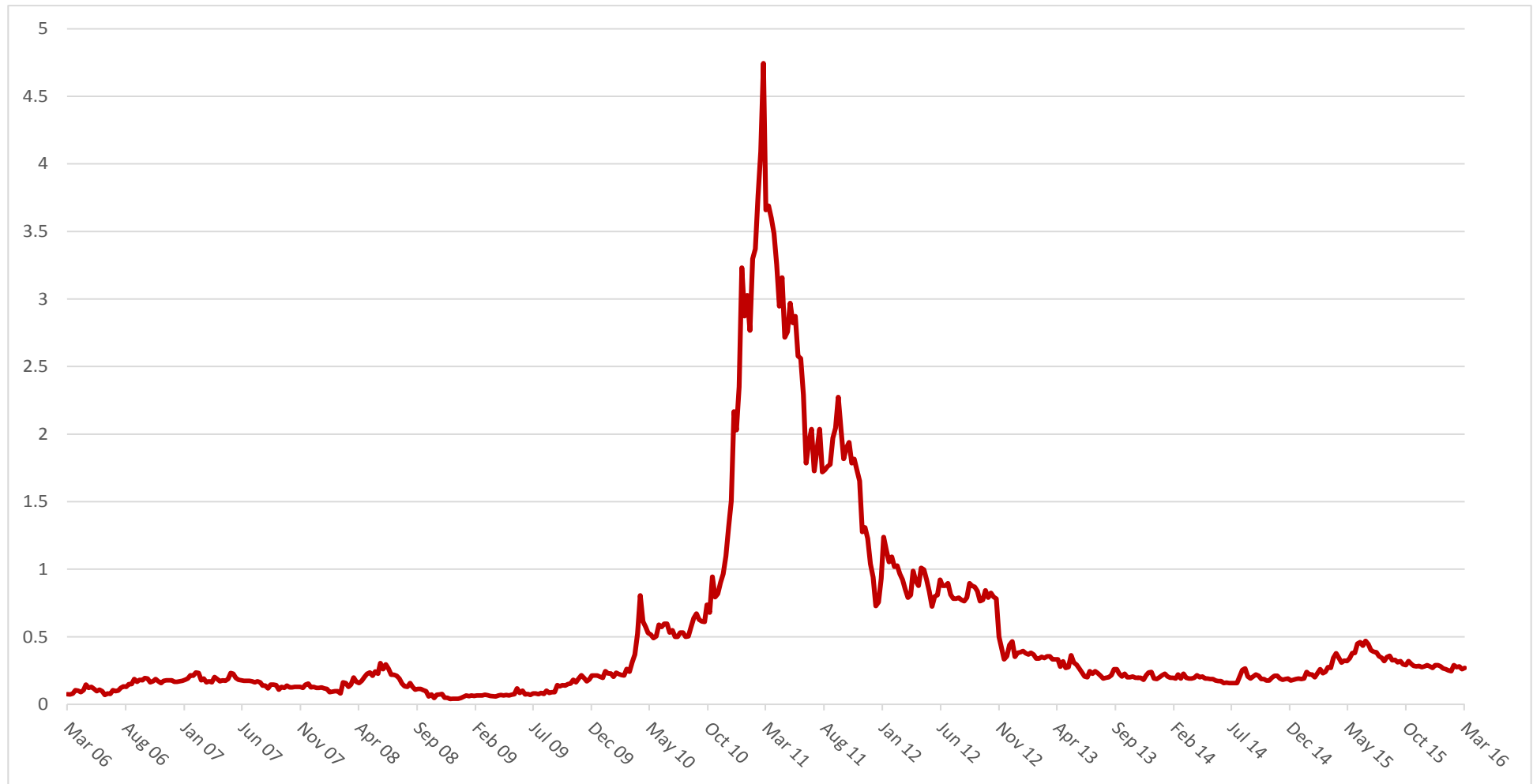
Source: WSJ

The new paradigm; this time it's different



GLENNON CAPITAL

SOUTHERN BOULDER



The deposit will extend at length and depth!

WHAT WE CAN LEARN FROM BUBBLES

- Buy real businesses at reasonable valuations
- Real business make a profit and generate cashflow
- The world doesn't change overnight
- Don't buy leaders that will become minnows
- Keeping an eye out for bubbles; investors buying stocks at
 - cyclically high revenues
 - unsustainably high margins
 - peak multiples

INVESTMENT CASE STUDIES

NATIONAL VETERINARY CARE LIMITED (ASX: NVL)

Overview

Operator of vet clinics across most states in Australia. Currently has 32 clinics. Attractive industry characteristic where the largest competitor only has 5.6% market share. Management are both ex-Greencross. The business has an acquisition model supplemented by a margin improvement process led by corporate initiatives.

Background

Listed on in August 2015
Listing on 8x PER

Revenue \$52.0m
Mkt Cap \$30.0m

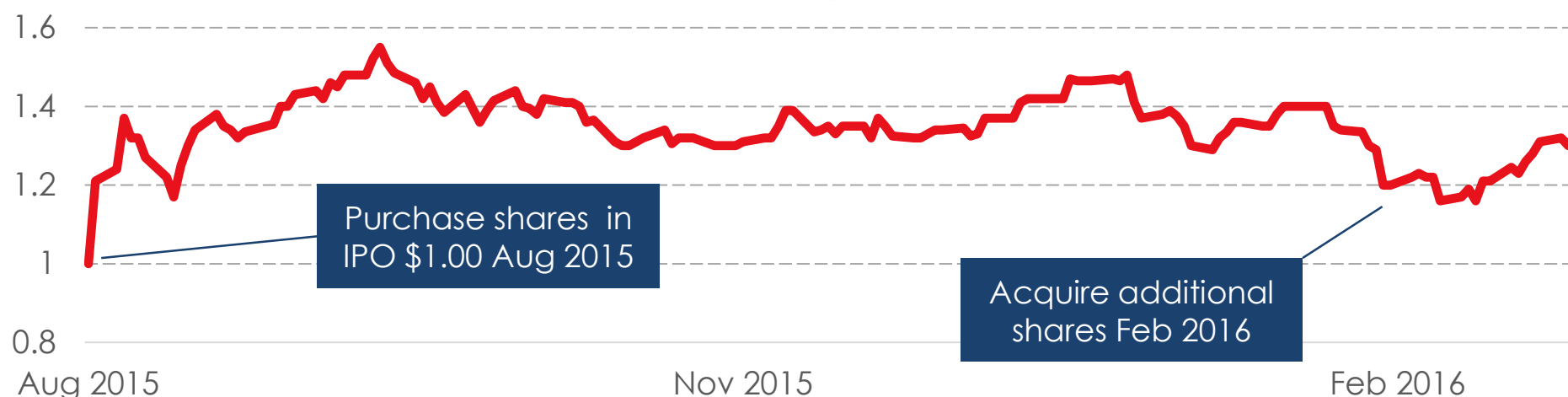
Thesis

Glennon Capital were an early investor in Greencross. We like the business model, the industry, the management and opportunity available for the company to expand. The business replicates the early Greencross model which appealed to us. The industry characteristics are favourable and barriers to entry are high. Management are both experienced and driven to succeed. Presently multiples for acquiring practices are reasonable and competition for practice acquisition is low.

Now

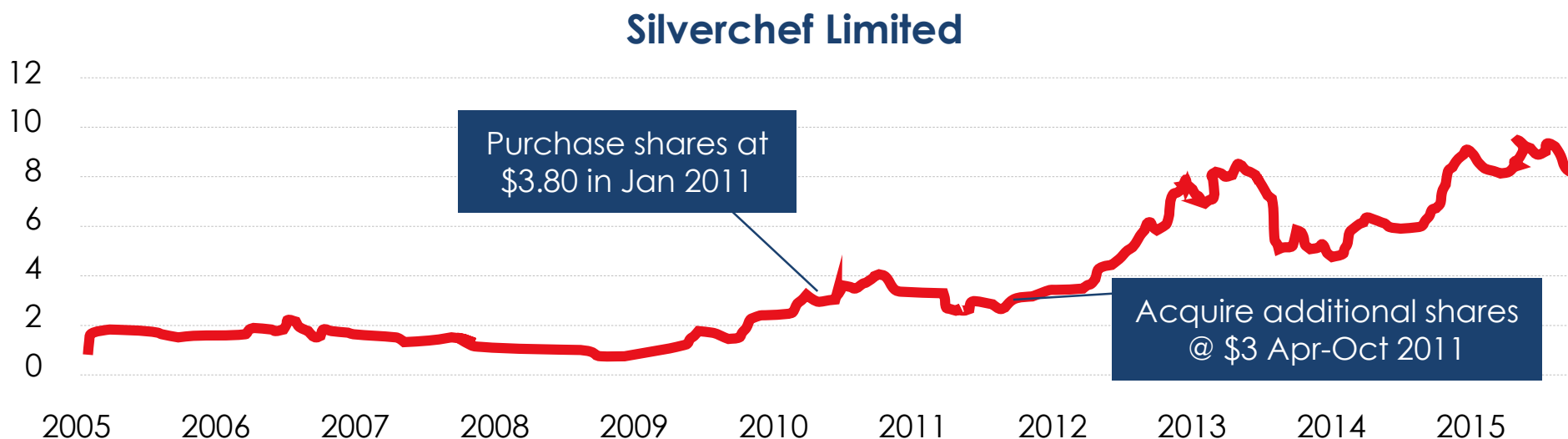
Trading on a FY16 PER of 10.0x
Mkt Cap \$60m

National Veterinary Care Limited



SILVERCHEF LIMITED (ASX:SIV)

Overview	Provider of finance to small and medium businesses. The business historically provided asset financing to the food industry for stainless steel kitchen fittings. The company has now expanded into other finance offerings, predominantly for capital items. They have also expanded internationally into both NZ and Canada.	
Background	Listed in 2005 Listing PER of 8x Revenue \$8m	Profit \$1.4m Mkt Cap \$11.1m
Thesis	Since 1988 large finance companies have been withdrawing from the Australian market. The traditional leasing companies have moved their product offerings into significantly higher value clients and have moved out of the SME sector. The Australian market is similar to Canada, however the market in Canada is not as advanced as Australia so there is opportunity for growth.	
Now	Mkt Cap \$300m Revenue \$200m	Profit \$18m Trading on a FY16 PER of 16x



CAPILANO (ASX:CZZ)

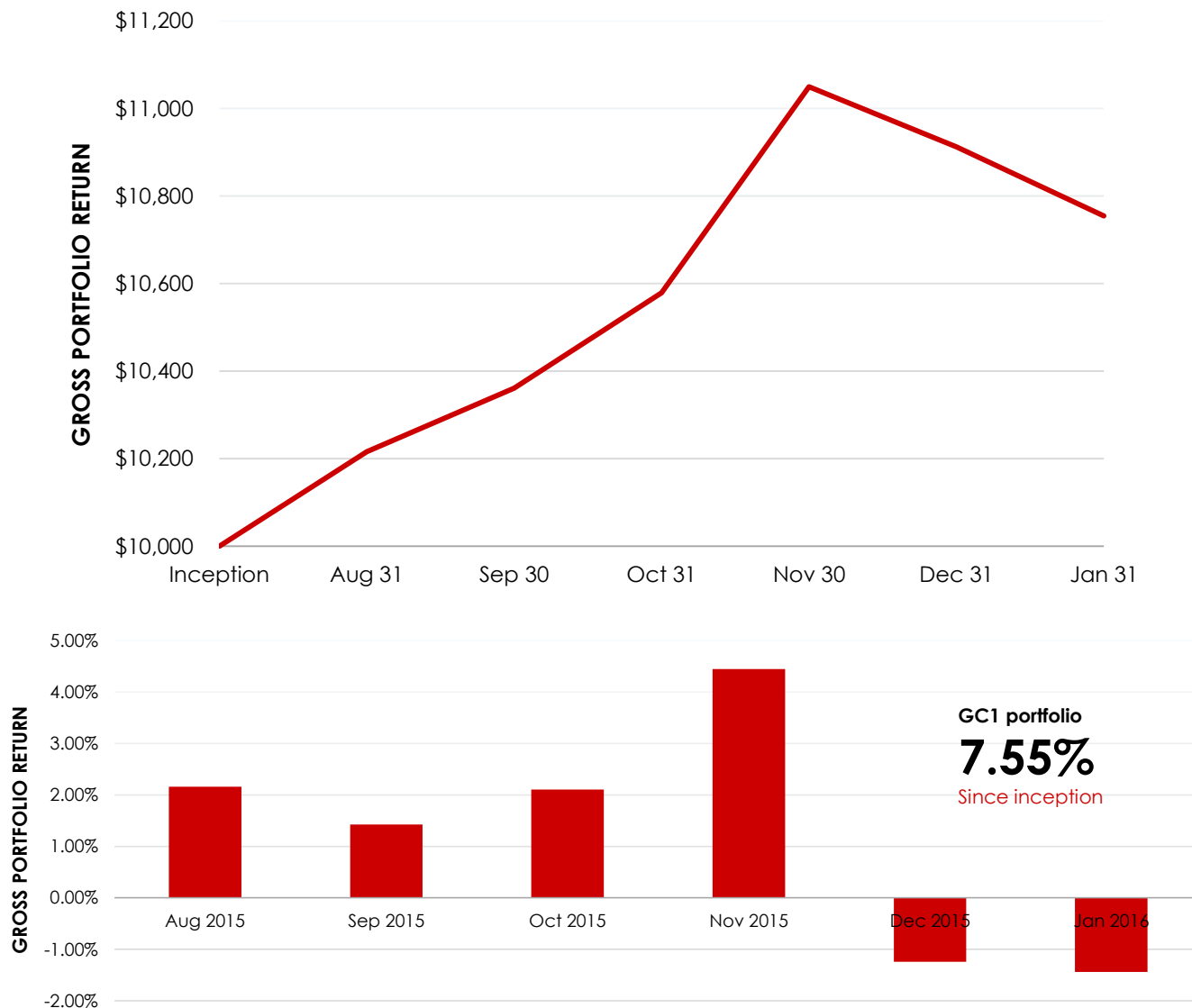
Overview	The business buys honey from beekeepers, processes and packages the honey, then sells branded products mostly to supermarkets. Capilano has a dominant 75% market share in domestic retail honey sales through brands such as Capilano, Allowrie and Wescobee, as well as a growing export business	
Background	Listed on ASX 2012 PER of 7x Revenue \$67m	Profit \$2.5m Mkt Cap \$17m
Thesis	Given Capilano's dominant position in the local market we would look for the company to benefit from organic growth in volume over time. And with this dominant position we don't believe increased supply would lead to an unwind in margins, as Capilano holds or improves margins over time. Operating leverage, an increase in exports (growing 29% last year) and increased sales of higher margin Manuka honey provide upside.	
Now	Mkt Cap \$159m Revenue \$145m	Profit \$12m Trading on a FY16 PER of 13x

Capilano Limited



INFORMATION ON GC1

GC1 PERFORMANCE



HOW TO BUY GC1

ONLINE

- ANY BROKER
- ETRADE
- COMMSEC

OFFLINE

- STOCK BROKERS
- FINANCIAL PLANNERS

PLATFORMS

- HUB24
- MACQUARIE WRAP
- LEVERAGE EQUITIES
- COLONIAL
- NETWEALTH

GLENNON WEEKLY NEWSLETTER



March 05, 2016

National Veterinary Care Limited

- We met with management of National Veterinary Care Limited last week, following the release of their first results announcement.
- Glennon Capital were early investors in Greencross and it would be interesting to have a look at this company to emulate some of the success of Greencross.
- Watch our video to find out more about NVL.

[Watch now](#)



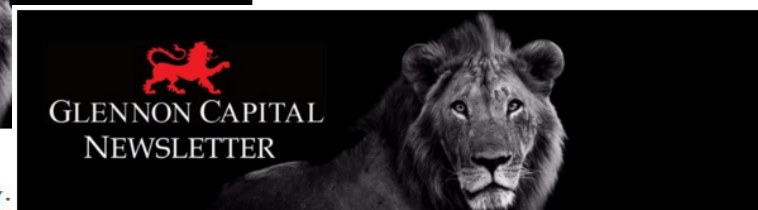
February 20, 2016

Insight | Paragon Care (ASX:PGC)

February 19, 2016 | By [Glennon Capital](#)

- Paragon is a distributor of consumables and capital equipment that has moved into the Australian healthcare market. The business is growing through acquisitions and consolidating a very fragmented market.
- To watch our video on Paragon, click on the link below

[Watch now](#)



January 30, 2016

Insight | Silver Chef Limited (ASX:SIV)

January 29, 2016 | By [Glennon Capital](#)



- Silver Chef Limited (ASX:SIV) is a small company that operates an equipment financing business predominantly for the food industry. The business is 30 years old and has been listed since 2005. In the past few years the company has expanded offshore and is starting to get good growth in Canada and New Zealand.
- The offering has also been expanded outside the food industry through the 'GoGetta' brand, which offers small loans to businesses, predominantly for equipment. The main benefit for Silver Chef clients is that financing allows them to avoid the need to make large up-front investments.

[Watch our video to learn more](#)



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INDEPENDENT COVERAGE



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QUESTIONS

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