NAOS Absolute Opportunities Company (NAC)

MONTHLY INVESTMENT REPORT AND NTA UPDATE

FEBRUARY 2016

NAOS

KEY CHARACTERISTICS

1. Global, Multi Asset Class Exposure
NAC invests in a range of equity, fixed income, currency and commodity securities both in Australia and Offshore, providing significant scope for capitalising on performance generating ideas. Key themes are identified and analysed for their impact at the security level, allowing the Investment Team to take advantage of fluctuations and mis-pricing situations on a cross sector, asset class and geographic basis.

2. Positive Absolute Return & Income Generation Focus
The primary focus of the Company's investment strategy is the preservation of shareholders capital and the generation of meaningful absolute returns with a lower downside volatility than traditional equity focused managed funds. NAC offers investors the opportunity to derive a targeted minimum dividend of 4% p.a., which will be franked to the maximum extent possible.

3. Focus on Meaningful Long Term Performance
Investment opportunities are assessed based on their potential to generate meaningful long term performance. Of primary consideration is quality rather than quantity, resulting in a concentrated portfolio of 'Best Ideas' (typically 0-30 holdings).

4. Ability to Hold +100% in Cash
It has been proven that holding cash offers the 'best hedge' during times of crisis. Holding cash also provides flexibility and nimbleness to take advantage of security mispricing opportunities as and when they arise.

5. Significant Alignment of Interests with Shareholders
NAOS employees/directors own a significant amount of shares and options in NAC. Staff are remunerated on the basis of the performance of the firm's investment vehicles through the application of a Performance Based Fee.

Net Tangible Asset Value Breakdown as at 29th February 2016

Pre Tax NTA:	$1.13
Post Tax & Pre Unrealised Gains NTA:	$1.14
Post Tax NTA:	$1.11

*The above NTA calculations do not account for any potential dilution from the 21,492,500 NACO options that remain on issue (expiry 30th November 2016) and which are exercisable at $1.00

Portfolio Performance & Positioning

The Naos Absolute Opportunities Company returned -1.02% for the month of February. This result was marginally better than global markets as the MSCI All Country World Index was -1.31% in AUD terms and the ASX All Ordinaries Accumulation Index was -1.47%.

February marked reporting season in Australia and we were very happy with how our companies reported. Despite the strength of the results from core holdings such as MNF Group, Event Hospitality, Smart Group and BWX Ltd we did not quite see the performance we expected from share prices and we believe this was partly due to the fact that some of the stocks we owned had become 'crowded' trades. We have reduced our weighting in Event Hospitality, but it still remains a sizeable position within the portfolio. Key positions within the rest of the portfolio remain broadly unchanged.

	1 Month	3 Month	6 Month	1 Year	Inception (p.a.)	Inception (Nom.)
NAC Investment Portfolio Performance*	-1.02%	+4.28%	+13.92%	+20.09%	17.37%	+23.11%
Benchmark (RBA Cash Rate + 250bps)	+0.39%	+1.20%	+2.37%	+4.84%	4.97%	+6.49%
Relative Performance	-1.41%	+3.08%	+11.55%	+15.25%	+12.40%	+16.62%
S&P/ASX All Ordinaries Accumulation Index (XAOAI)	-1.47%	-4.31%	-3.09%	-12.23%	-3.08%	-3.98%
MSCI ACWI (Net, Dividends Reinvested, AUD Terms)	-1.31%	-7.39%	-6.14%	-4.04%	+7.96%	+10.45%

*Investment Portfolio Performance is post all operating expenses, before fees and taxes.

Market Insight

Reporting season is a great time for us to catch up with many of Australia's listed company CEO's which gives us a cross sectional view into how the Australian and the global economy is performing. Further to meeting with them we spend huge quantities of time reading transcripts from conference calls. Below we provide some of our favourite quotes from the CEO's and how they are seeing conditions at present;

Currency is hurting gross margins in retail…

"Currency is driving us obviously and is impacting the landed price for our suppliers in Australia" **JB Hi-Fi (Electronic Goods)**

"Our gross profit margin is lower than pcp which has been impacted by the weaker Australian dollar" **Woolworths South Africa (recently bought David Jones and Country Road)**

"Supplier price increases occurred as a result of the lower Australian dollar" **Burson (Auto parts retailer)**

BUT the currency is helping exports and tourism…

"We are seeing favourable pricing conditions at the moment and obviously a depreciating Aussie dollar helped the actual margin" **Tassal Group (Salmon Farmer)**

"Through the business and private bank we are starting to see some signs of the low Australian dollar on some export-sensitive industries such as education, tourism, niche manufacturing and agriculture" **CBA (Bank)**

"A series of free trade agreements and a depreciating currency were significant factors in this improved export performance" **Australian Vintage (Wine producer)**

Credit conditions are tightening on residential lending…

"We've tightened our scorecard around things like residential development" **CBA (Bank)**

"Overall the high loan-to-value market in the 80-90% space is down about 8% through September. We also saw investment property growth level off in the third quarter and was down almost 20% from second quarter to third quarter" **Genworth (Mortgage Insurance)**

BUT the residential market still remains strong…

"Metro Sydney we expect volumes to continue at similar levels to what we currently are experiencing. However, price growth will be limited as we meet some affordability challenges. In Metro Melbourne, we're expecting strong volumes there to continue and that's really on the back of good strong population growth and a strong labour market. That is a well supplied market so expect subdued price growth there. In Southeast Queensland, we're also seeing good trading levels continue and that Southeast corner in particular is supported by good relative affordability and also a rebound in tourism" **Stockland (Residential REIT)**

The ageing population theme remains intact…

"One in three people over the age of 65 have some type of hearing loss. If you think about from a ageing population perspective those dynamics are very much in our favour from a business perspective, because hearing loss from people over the age is 60 is one of the leading health concerns, so one in three being over the age of 65 having hearing loss really fits into our wheelhouse." **Cochlear (Hearing aids)**

"The population is aging in most countries around the world. Sadly, for those of us who are part of it, there is an absolute correlation between age and utilization of health care. And that continues apace and will continue apace for many years to come" **Ramsay Healthcare (Hospitals)**

There is significant growth in passive funds management vs active…

"Once again, passive flows dominated delivering 11% in terms of new business growth on the year" **Henderson Group (Fund Manager)**

"Last year, index funds were allocated nearly 20% of every dollar invested in the market. That is up from 10% fifteen years ago. While we would not yet describe the current phenomenon as an index fund bubble, it shares similar characteristics with other market bubbles" **Bill Ackman (Fund Manager)**

Miners haven't stopped targeting cost-out…

"Operating cost reductions are the most significant lever to protect the business and the cash flows, and the focus on this must remain relentless. The reductions we're targeting are becoming much more challenging but we believe that we can take around $2 billion out of our cost base over the next two years. We're targeting a step-down in the service and support cost areas" **Rio Tinto (Diversified Mining)**

"There are also some important controllable factors I'd like to draw your attention to. We've spoken before of the tireless efforts of our people to safely improve productivity, and having already unlocked annualized savings of more than $10 billion over the last three years, our businesses have continued to improve productivity. We've lowered our unit costs even further in the current period, and there's still much more to come" **BHP (Diversified Mining)**

In addition to the anecdotes provided above, Deloitte have compiled a set of reporting season stats which we have re-printed below.

- 66% of non-resources companies increased their earnings
- 49% of all companies beat expectations (the norm is 45%)
- 67% of companies outperformed the market on the day they reported (usually it is half)
- 63% of companies increased their dividend

Overall we think the recent sell-off in the market will provide us with the opportunity to find new positions for the fund as well as adding to our existing holdings where appropriate.

Positive Stock Attribution Analysis (12th November 2014 to 29th February 2016)

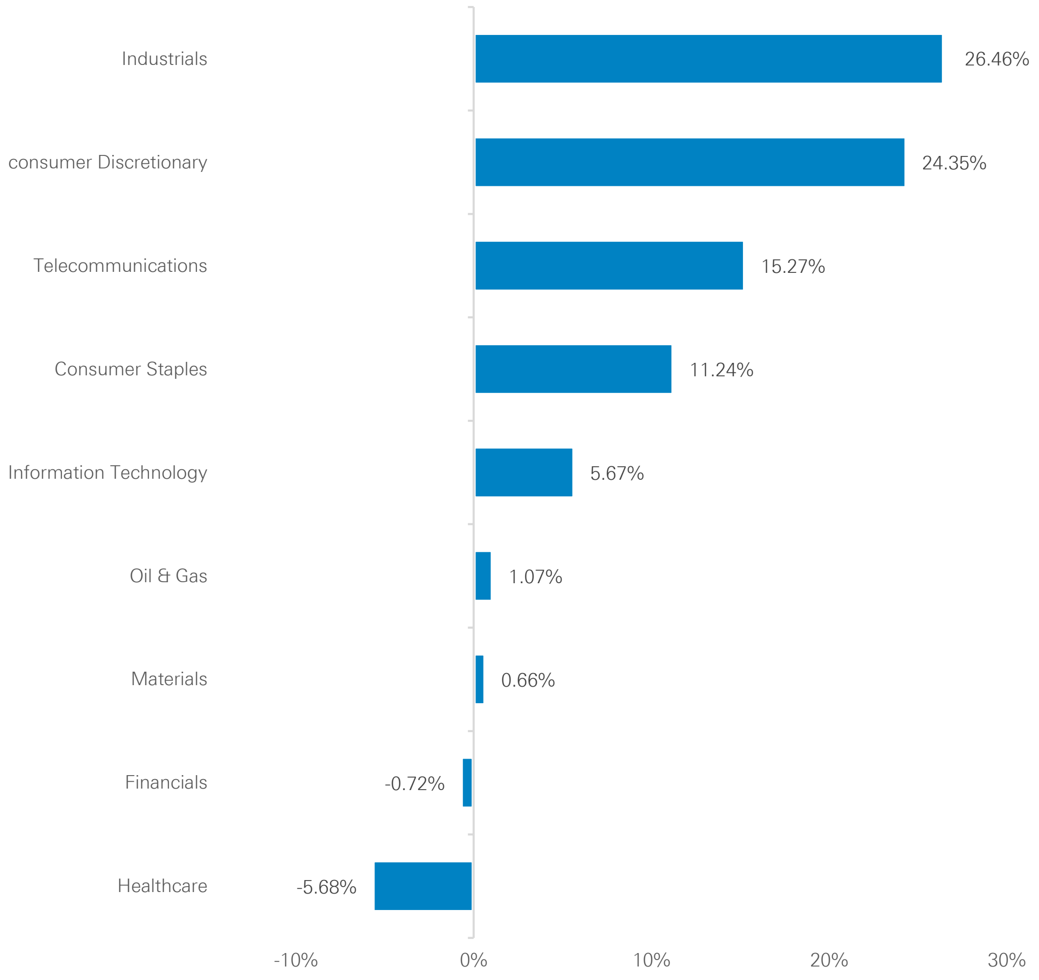
Below is a table listing the top positive contributors to NAC's total return since inception. The purpose of the table is to illustrate that the performance the investment team derive over time is not simply from one or two positions, but from a variety of positions, even with a concentrated portfolio of investments that is generally limited to 0-40 securities at any one time. Positions in the table below may have been held either as a long position or short position at any given point in time.

Investment	Contribution to Return (%NAV)	Investment	Contribution to Return (%NAV)
US Dollar	+7.03%	Bellamy's Australia	+2.12%
Event Hospitality	+4.02%	Macquarie Atlas Roads	+2.10%
Sirtex Medical Limited	+2.84%	I-select Limited	+1.59%
Enero Group	+2.27%	BWX Limited	+1.50%

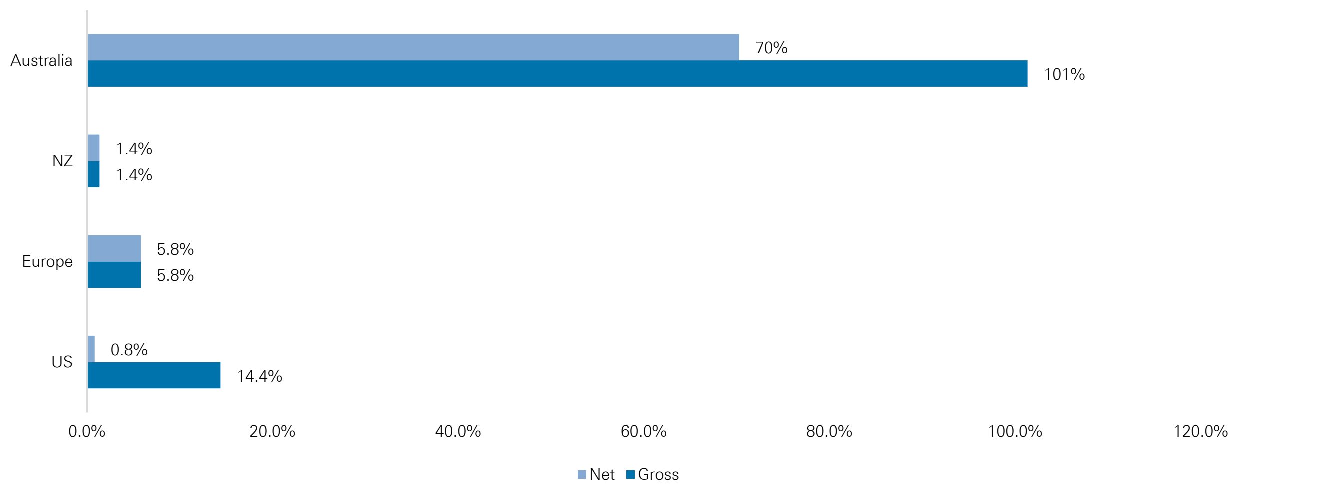
Portfolio Analysis as at 29th February 2016

As at 29th February the portfolio comprised of 43 holdings, including 31 long equity positions, 8 short equity positions and 4 income instruments.

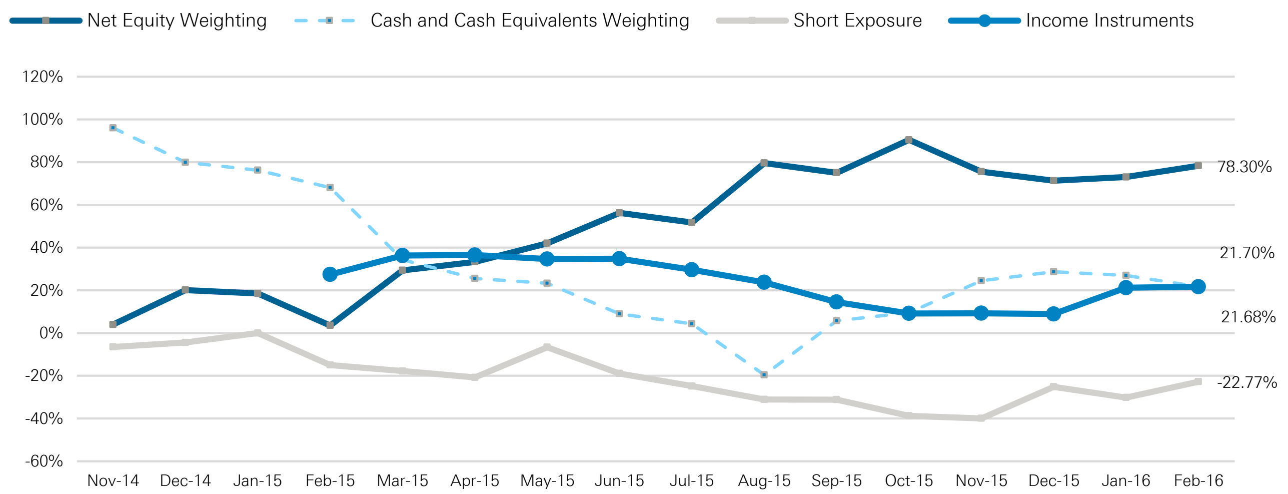
Net Industry Exposure



Gross Geographical Equity Exposure



Net Equity Exposure



Company Meetings

The NAOS investment philosophy is based around the belief that for a company to succeed and generate strong returns for shareholders it must be led by a motivated, proven and experienced management team. That is why the NAOS Investment Team has contact with many listed and unlisted companies across a wide range of industries and geographies. A selection of the unlisted and listed companies the team had contact with during the month of February were as follows:

- Event Hospitality (EVT AU)
- Smart Group (SIQ AU)
- AP Eagers (APE AU)
- Select Harvest (SHV AU)
- Broadspectrum (BRS AU)
- REA Group (REA AU)
- BWX Ltd (BWX AU)
- Domino's Pizza (DMP AU)
- The Reject Shop (TRS AU)
- MNF Group (MNF AU)
- Estia Health (EHE AU)
- Automotive Holdings (AHG AU)

Portfolio Characteristics – Summary Data as at 29th February 2016

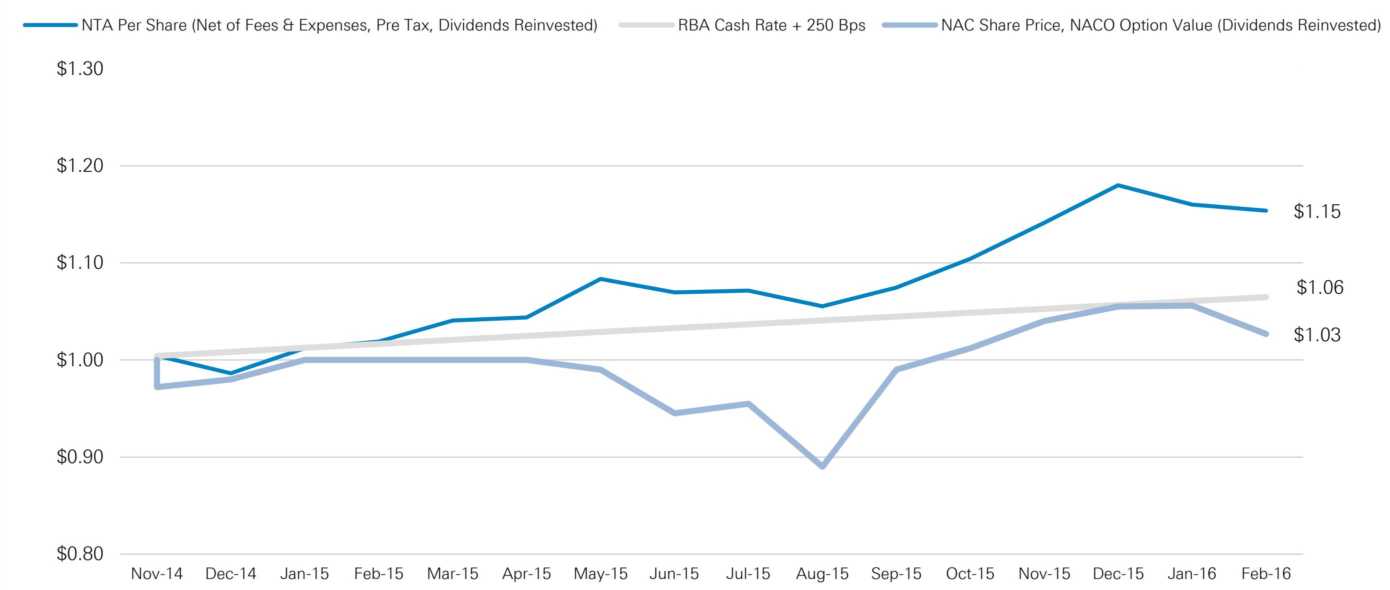
Total Number of Equity Holdings (Long & Short)	39
Total Number of Income/Debt Instruments*	4
Total Number of Holdings	43
Portfolio Weighted Market Capitalisation (AUD)	$14.25bn
Percentage of Positive Months (NAC)	69%
Percentage of Positive Months (XAOAI)	44%
Standard Deviation of Returns (NAC)	9.34%
Standard Deviation of Returns (XAOAI)	13.33%
Correlation of Returns to XAOAI	0.47N
Sortino Ratio	6.43
Downside Deviation (NAC)	2.70%
Downside Deviation (XAOAI)	7.95%
Current Estimated Portfolio Beta	0.145

*Listed and unlisted bonds, convertible notes, preference shares and other income securities – both domestic and international.

Capital Management - Summary Data as at 29th February 2016

Share Price	$0.965
Share Price Discount to NTA (undiluted, pre tax)	14.60%
Historical Fully Franked Dividend Yield	4.66%
Historical Gross Dividend Yield	6.66%
Shares on Issues	21,507,500
Options on Issue	21,492,500
Directors Shareholding	1,480,203

NTA & Share Price Analysis



Description of Statistical Terms/Glossary

Portfolio Weighted 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 securities move in relation to each other. In this case the two securities are NAC and XAOAI. If the correlation is 1 then the two securities should have the same monthly returns and if the correlation is -1 and XAOAI had a return of -1.00% then NAC 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 may potentially indicate that there is a low probability of a large capital loss.

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.

XAOAI – All Ordinaries Accumulation Index

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Warwick Evans (Director)
Sebastian Evans (Director)

Company Secretary
Julie Coventry

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