NAOS Absolute Opportunities Company (NAC)

MONTHLY INVESTMENT REPORT AND NTA UPDATE

MARCH 2016

N Λ O S

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 shareholder's 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 31st March 2016

(Pre the Payment of $0.0225 Fully Franked Dividend Ex on 19th April 2016)

Pre Tax NTA:	$1.19
Post Tax & Pre Unrealised Gains NTA:	$1.19
Post Tax NTA:	$1.15

*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

Investment Portfolio Performance & Positioning to 31st March 2016

The Naos Absolute Opportunities portfolio returned +5.97% for the month of March. For the quarter, the investment portfolio finished +2.38%. This compares to the ASX 200 Accumulation Index which finished -2.75% for the quarter, the MSCI All Companies World Index which was -0.28%, while the S&P 500 finished in positive territory at +0.77%.

Despite what the March closing figures for most major indices will tell you, the first quarter of 2016 was extremely volatile. By the 20th of January the S&P 500 had fallen 11.3% and by early February the ASX had followed suit hitting a low of -11.1% from its high. Wall Street Weekly reported that "the Dow did something it hadn't done since the Great Depression. It fell by more than 10% before finishing the same quarter with a gain of more than 1%."

The main contributors to performance came from selected short positions in low quality technology stocks which had become significantly overvalued in our view. Further contributions came from long positions in Smart Group, Billabong and Moleskin SpA (Italian listed).

	1 Month	3 Month	6 Month	1 Year	Inception (p.a.)	Inception (Nom.)
NAC Investment Portfolio Performance*	+5.97%	+2.38%	+18.38%	+23.87%	+21.20%	+30.45%
Benchmark (RBA Cash Rate + 250bps)	+0.41%	+1.21%	+2.40%	+4.83%	+4.96%	+6.93%
Relative Performance	+5.56%	+1.17%	+15.98%	+19.04%	+16.24%	+23.52%
S&P/ASX All Ordinaries Accumulation Index (XAOAI)	+4.74%	-2.35%	+4.11%	-8.05%	+0.42%	+0.58%
MSCI ACWI (Net, Dividends Reinvested, AUD Terms)	+0.32%	-4.57%	-3.57%	-4.96%	+7.70%	+10.81%

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

Market Insight

The volatility in Australia has stemmed mainly from a few key sectors which make up a large part of the index. The Australian financials sector, including the big four and the regional banks makes up approximately 46% of the ASX200 index. The issue with the financials at present however is that investors are fearing we are in the early stages of a bad debt cycle. For the past few years bad debts for the banks have been low as we have had a buoyant housing sector and affordable interest rates. Each year banks make provisions for bad debts and when those provisions are not utilised they are added back to profits. This has been going on for a few years now and has created the appearance of strong profits, despite the underlying numbers not being so.

In the second half of 2015, the banks started raising interest rates for investor home loans. This was an out of cycle move where there has been no change to the Australian cash rate but the banks have put their lending rates up. Now the banks are starting to push owner-occupied lending rates higher. They have done this in an effort to protect their margins, although in the process they have made it more difficult for borrowers to repay their debt. ANZ and WBC both recently announced that bad debt provisions will be increased which is the primary cause for concern that the buoyant conditions we have seen in the last few years may not be here to stay. As a result, the banks underperformed the rest of the market despite their heavy index weighting.

On the other end of the Australian market 'barbell' is a combination of the materials sector (which includes the large Australian miners) which makes up approximately 13% of the index and the energy sector which adds another 4%. The price of crude oil has traded in a range between $60 and $26 over the past 12 months since falling from over $100 in 2014. Due to the rapid fall in price, investors have unsparingly sold their positions in energy stocks leaving them significantly out of favour. The issue when a sector is so unloved and so under-owned is that it doesn't take much of a media headline or a move in the underlying commodity price for investors to quickly play catch up. It is very common at the moment for the price of oil to move +/- 2% overnight which has been causing some of the oil stocks to trade +/- 10% the following morning. This is a very difficult environment to be investing in and being caught on the wrong side of such a move can be very damaging to portfolios.

Figure 1 below shows the price of crude oil (in the top half of the chart) and the volume traded (in the bottom half of the chart). As you can see with such a rapid fall, volume has increased significantly which is the cause of a lot of the volatility.

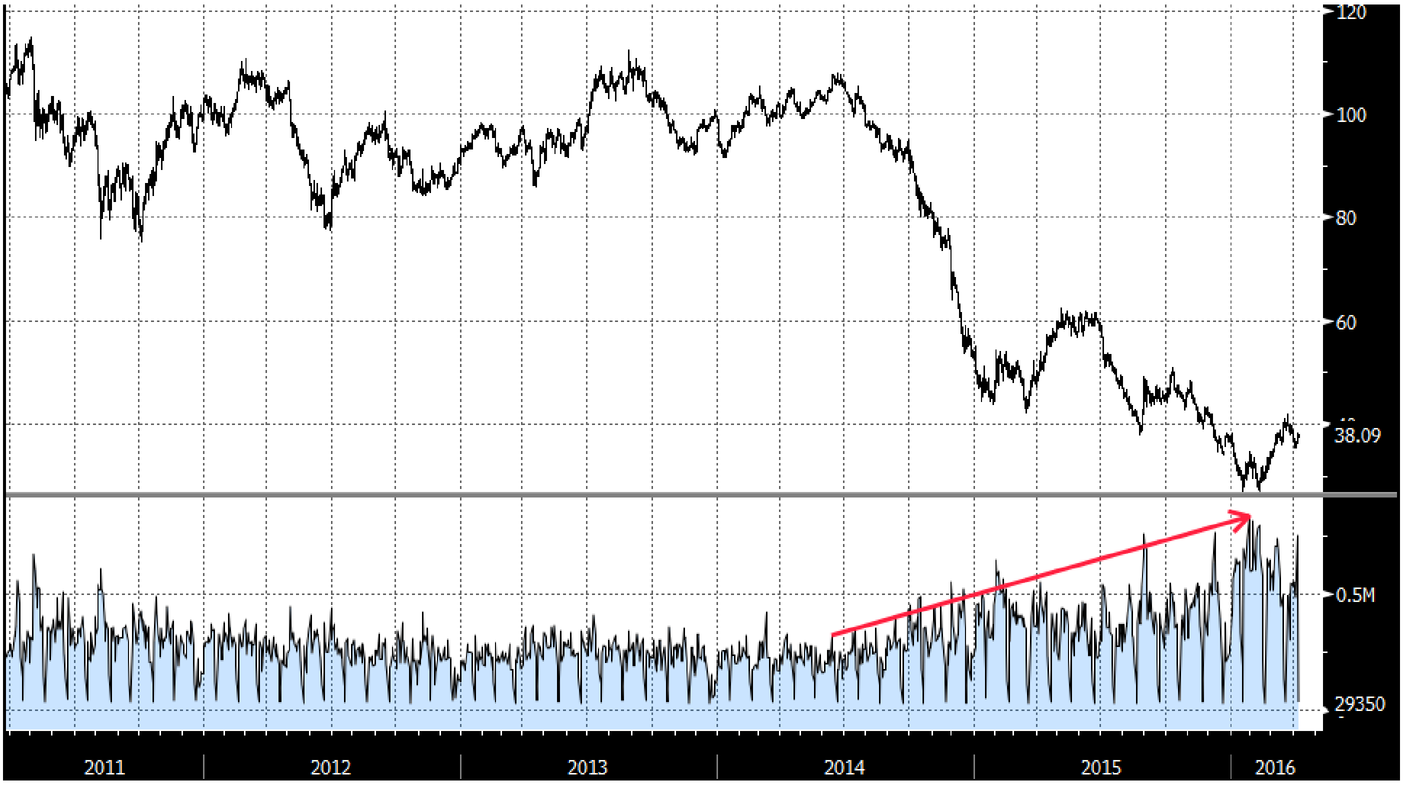


Figure 1: Chart of Crude Oil
Source: Bloomberg

Similarly, other commodity stocks have been a very 'under-owned' part of the market due to a consensus view that the wash out from the commodities super cycle has not yet run its course. However as part of that we have a gold sector that has been benefitting from a falling $A (as gold is priced in US dollars the Australian producers receive more on their sales) as well as investors buying the metal looking for a safe haven. Further, the price of iron ore has been rallying as Chinese mills go through a re-stocking cycle and the Chinese Government has injected further stimulus into capital spending. With a situation not dissimilar to the energy market which we have talked about above, it creates significant volatility and makes for a difficult environment to be investing.

To date we have been able to keep the volatility of the Naos Absolute Opportunities portfolio low. This can be seen in our standard deviation of returns which we publish each month and we find a useful indicator for tracking this volatility. Currently our portfolio standard deviation is at 9.82% vs the ASX all ordinaries accumulation index of 13.54%. While we expect the volatility in the markets to continue we see it more as an opportunity to acquire stocks at reasonable valuations rather than a worrying sign for our portfolio.

Positive Stock Attribution Analysis (12th November 2014 to 31st March 2016)

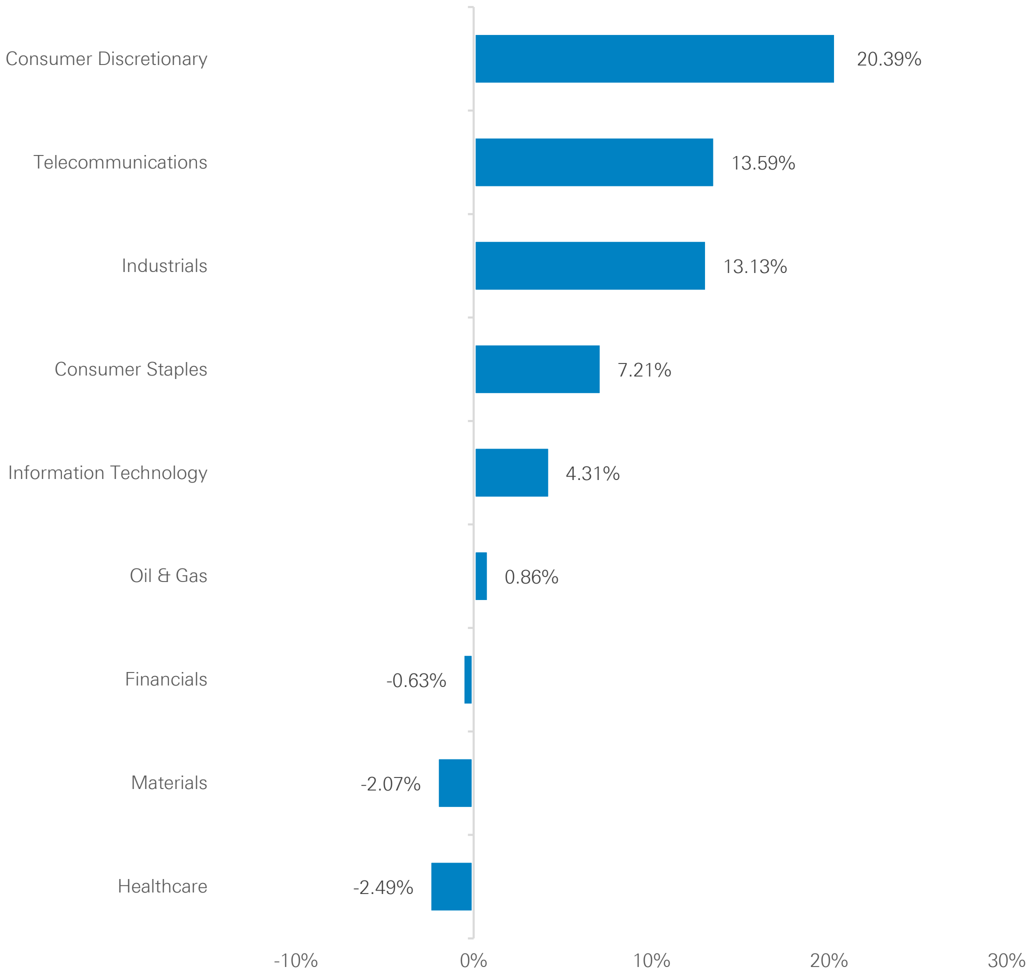
Below is a table listing the top positive contributors to NAC's total return since inception. The purpose of the table is to illustrate that the performance the investment team derive over time is not simply from one or two positions, but from a variety of positions, even with a concentrated portfolio 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	+7.35%	1-Page Ltd	+2.85%
Event Hospitality	+4.09%	Macquarie Atlas Roads	+2.25%
Enero Group	+3.13%	Bellamy's Australia	+2.23%
Sirtex Medical	+3.07%	Smart Group	+2.11%

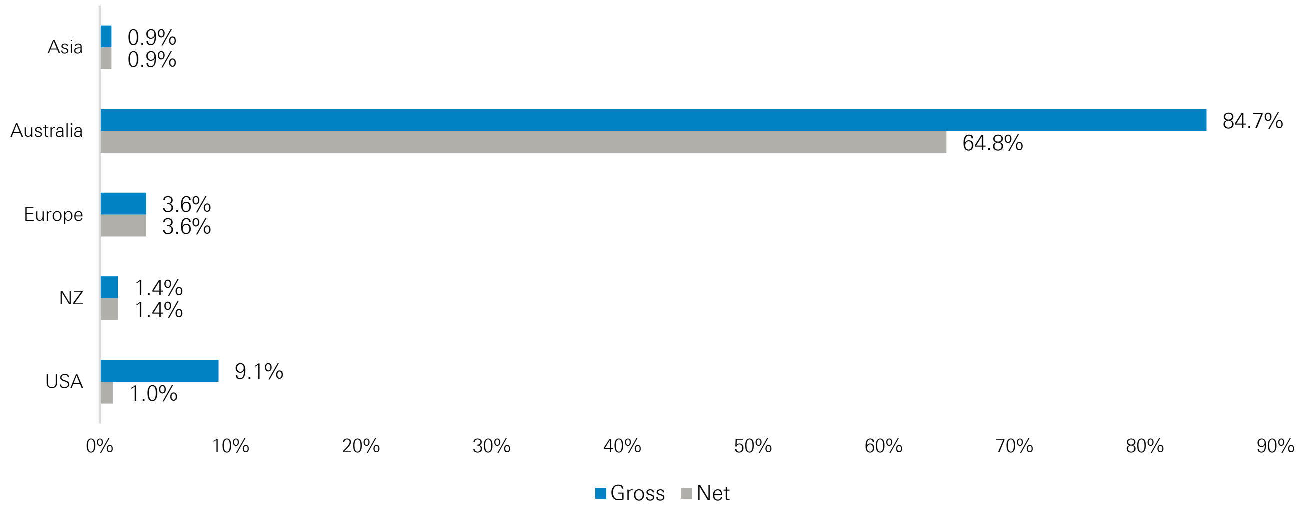
Portfolio Analysis as at 31st March 2016

As at 31st March the portfolio comprised of 40 holdings, including 26 long equity positions, 10 short equity positions and 4 income instruments.

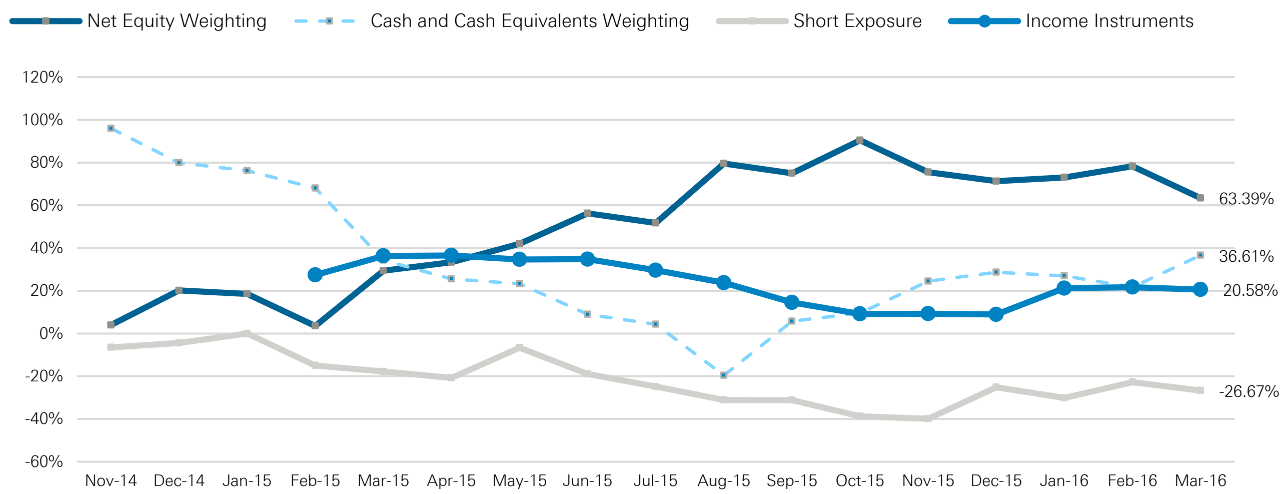
Net Industry Exposure



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 March were as follows:

- Monadelphous Group (MND AU)
- Surfstitch Group (SRF AU)
- Billabong International (BBG AU)
- Vitaco Limited (VIT AU)
- Bellamy's Australia (BAL AU)
- Caterpillar Inc (CAT US)
- Moleskin SpA (MSK IM)
- Trilogy International (TIL NZ)
- Vita Group (VTG AU)
- Sirtex Medical (SRX AU)
- Village Roadshow (VRL AU)
- Amaysim (AYS AU)

Portfolio Characteristics – Summary Data as at 31st March 2016

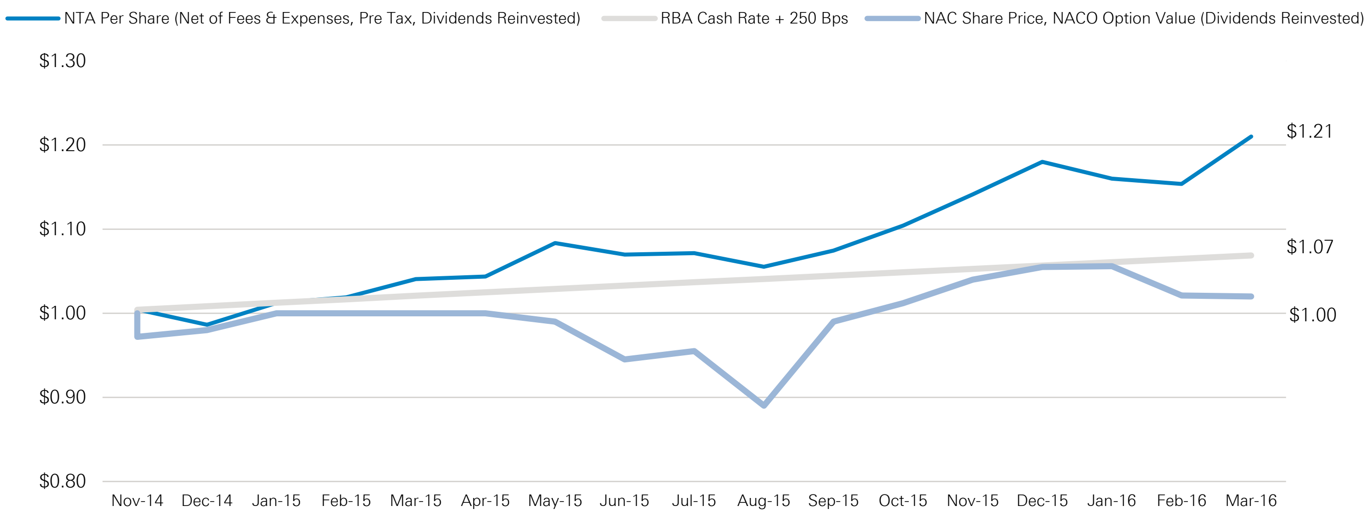
Total Number of Equity Holdings (Long & Short)	36
Total Number of Income/Debt Instruments*	4
Total Number of Holdings	40
Portfolio Weighted Market Capitalisation (AUD)	$15.49bn
Percentage of Positive Months (NAC)	71%
Percentage of Positive Months (XAOAI)	47%
Standard Deviation of Returns (NAC)	9.82%
Standard Deviation of Returns (XAOAI)	13.54%
Correlation of Returns to XAOAI	0.53
Sortino Ratio	7.99
Downside Deviation (NAC)	2.65%
Downside Deviation (XAOAI)	7.83%
Current Estimated Portfolio Beta	-0.11

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

Capital Management - Summary Data as at 31st March 2016

Share Price	$0.99
Share Price Discount/Premium to NTA (Undiluted, Pre-Tax)	-20.20%
Historical Fully Franked Dividend Yield	4.54%
Historical Gross Dividend Yield	6.49%
Shares on Issue	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

Disclaimer:
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Sebastian Evans (Director)

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