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Ganes Focused Value Fund *ARSN 117 119 712*
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GANES
CAPITAL MANAGEMENT LTD

GANES FOCUSED VALUE FUND – JUNE 2016

Unit Prices*

	30.06.16	30.06.15	30.06.14	30.06.13	30.06.12	30.06.11	30.06.10	30.06.09	30.06.08
Entry Price ($)	$2.6379	$2.5890	$2.5716	$2.4721	$2.0377	$2.0438	$1.8024	$1.5322	$1.8130
Unit Price ($)	**$2.6287**	**$2.5800**	**$2.5626**	**$2.4635**	**$2.0306**	**$2.0366**	**$1.7961**	**$1.5268**	**$1.8067**
Exit Price ($)	$2.6195	$2.5709	$2.5537	$2.4549	$2.0235	$2.0295	$1.7898	$1.5215	$1.8003
Distribution (cents per unit)	**8.8129**	**8.0993**	**4.0178**	**4.5014**	**4.8340**	**6.7378**	**5.8396**	**6.6702**	**11.6800**

* Unit prices are quoted pre-distribution. The *total* distribution paid during the financial year is shown.

Past Performance*

	Ganes Focused Value Fund	ASX300 Accumulation Index	Margin
3 months	2.2%	4.0%	-1.8%
6 months	-4.0%	1.2%	-5.2%
1 Year	4.8%	0.9%	3.9%
2 Years (p.a. compound)	3.7%	3.2%	0.5%
3 Years (p.a. compound)	4.4%	7.7%	-3.3%
5 Years (p.a. compound)	7.7%	7.2%	0.5%
7 Years (p.a. compound)	11.4%	8.7%	2.7%
10 Years (p.a. compound)	6.7%	4.8%	1.9%
13 Years (p.a. compound)	11.2%	8.9%	2.3%
Value of $10,000 invested at inception (14/10/2002)	**$43,791**	**$31,969**	

Largest Ten Holdings
Reece Australia (REH)
Clydesdale Bank (CYB)
Smartgroup (SIQ)
Beacon Lighting (BLX)
ARB Corporation (ARB)
Nick Scali (NCK)
PM Capital Global Opportunities (PGF)
Flight Centre (FLT)
Trade Me Group (TME)
Magellan Flagship Fund (MFF)

Portfolio Allocation

Top ten	50.5%
Other shares	45.6%
Cash	3.9%

* Fund performance is net of all fees and expenses, and assumes reinvestment of distributions. Investments can rise and fall in value. Past performance is not necessarily indicative of future performance. The fund currently invests substantially in smaller companies that may involve unique risks. The Product Disclosure Statement details the risks associated with an investment in the fund and is essential reading for investors.

The 2016 financial year has been a roller-coaster ride for investors with three notable sell-offs in August 2015, January 2016 and June 2016, but the end product was the market finishing the year more or less where it started.

It is very challenging for investors to keep their heads and stick to their long-term plan in periods like this. The relentless noise from the market and from commentators can be hard to ignore and some investors will find themselves doing long-term damage to their future wealth by reacting to this constant stream of news headlines. As professional investors we are closely connected to the markets each and every day, and so are even more exposed to the noise than most. However, over the years we have learnt to see this for what it is, a distraction to a sound long-term plan rather than information to be acted upon. Our plan centres on managing a portfolio of quality businesses with good long-term growth prospects for revenue and profits, and monitoring their achievement from year to year.

Financial Year	Ganes Return	ASX300 Return	Difference
2004	33.2%	21.7%	11.5%
2005	15.5%	26.0%	-10.5%
2006	34.8%	24.0%	10.8%
2007	45.0%	29.2%	15.8%
2008	-27.6%	-13.7%	-13.9%
2009	-14.1%	-20.3%	6.2%
2010	24.5%	13.1%	11.4%
2011	17.8%	11.9%	5.9%
2012	2.9%	-7.0%	9.9%
2013	23.7%	21.9%	1.8%
2014	5.6%	17.3%	-11.7%
2015	2.6%	5.6%	-3.0%
2016	4.8%	0.9%	3.9%

The Fund has reported its seventh year in a row of positive returns though again this year that return was a modest 4.8%. On a positive note, the Fund outperformed the market by 3.9% after two years of relative underperformance.

As is our regular practice in this end of financial year update we glance back to the ten largest holdings, which are suggestive of our best ideas one year ago, and see how these contributed to Fund performance over the year. The accompanying table indicates quite a mixed bag with strong double-digit returns from Austbrokers, ARB Corporation, and Cochlear, but large negative returns from Beacon Lighting, Lifehealthcare Group and GBST.

The insurance broking sector has been a difficult place to be over the last two or three years with insurance premiums under pressure which has been reflected in stagnant earnings at **Austbrokers**. While premium declines have stabilised, the outlook for the business is still subdued. We have gradually trimmed the portfolio holding since 2013 and it now sits outside the top ten holdings.

ARB Corporation has also experienced a subdued two or three years with profit margins compressing slightly after expanding appreciably over several years assisted by the resource sector boom. However, management at ARB are singularly focused on the long term and have invested heavily in new products and overseas infrastructure. With this investment expected to bear fruit over the coming years and the market driving ARB shares higher in expectation of this, ARB remains one of the largest holdings in the portfolio.

Top 10 stocks as at June 2015			
	% of portfolio (June 2015)	Total Return FY16	% of portfolio (June 2016)
Flight Centre	9.3%	-2.8%	4.6%
Templeton Global Growth	5.6%	-8.4%	3.1%
Austbrokers	4.9%	16.6%	3.5%
Sonic Healthcare	4.5%	4.2%	0.0%
Magellan Flagship Fund	4.0%	6.8%	4.4%
ARB Corporation	3.7%	30.8%	5.2%
Cochlear	3.5%	53.9%	3.7%
Beacon Lighting	3.4%	-29.7%	5.3%
Lifehealthcare Group	3.3%	-49.0%	0.0%
GBST	3.2%	-25.8%	3.0%

Cochlear delivered a 30% increase in EBIT at its half year result in February with recent new product launches driving demand and pushing the product recall difficulties of several years ago into the past. Reported revenue and profitability has also benefited from the depreciating Australian dollar. In response the market has pushed the share price of Cochlear sharply higher and the stock is currently firmly entrenched in the top ten holding of the portfolio.

The **Beacon Lighting** share price was hit hard in May this year when the company released a trading update which downgraded sales and profit expectations for the full year due to a raft of causes including the timing of the Easter break, weak consumer confidence, an increase in clearance activity by competitors (eg. Masters hardware) and reduced advertising. While we don't like to see such a lengthy list of 'excuses' we note it was always going to be difficult for the company to back up after very strong growth in the FY15 results. We are also reassured by the ongoing management role of the founders and their significant personal stake in the company. We took the share price weakness as an opportunity to increase the Fund's holding.

Earlier in the year **Lifehealthcare** surprised us with a weaker result than expected including very poor cashflow for the period. Following a change of management this gave us cause for concern and we took the decision to exit the investment. **GBST** shares also ended the year much lower than where they started having been hit by a profit warning in October last year and then being caught up in the Brexit fall-out in June with their exposure in their business to the UK market.

By far the biggest winner for the portfolio over the year was the salary packaging and novated leasing business **Smartgroup** which started the year with a share price of $2.20 and finished at $5.75 pushing it firmly into the top ten holdings. The share price has benefited from strong revenue and profit growth driven by both organic initiatives and acquisitions. Stocks like Smartgroup have also benefited from a reduction in regulatory risk as both major parties publicly committed to maintaining the current favourable salary packaging and Fringe Benefits Tax measures during the election campaign. However, as we are well aware, politicians are apt to change their minds so this remains a longer term risk.

Clydesdale Bank was added to the portfolio earlier in the year following its divestiture by the National Australia Bank, and is now also a top ten holding. Clydesdale is a British bank focused on the retail and SME markets in Northern England, the Midlands and Scotland. CEO David Duffy was installed in June 2015 to manage the demerger from NAB and, having orchestrated a major turnaround at Allied Irish Bank, is being relied on to achieve something similar at Clydesdale. At listing, Clydesdale traded on just 0.6 times book value, reflecting the low level of profitability and high cost to income ratio in the business. Our view is that Duffy will be able to achieve this and see the shares re-rate back toward book value. After taking an initial position around $4 per share, the share price rose quickly to $5.80 following the release of its half year results in May before being smacked down by the shock Brexit vote at the end of June and its implications for the local UK economy and property prices.

We are optimistic about the future prospects of the portfolio of businesses held by the Fund and this is reflected in the fully invested position of the fund over the past twelve months. The portfolio comprises a mixture of smaller and mid-cap companies with motivated and innovative managers, good revenue and profit growth potential, as well as strong balance sheets and healthy cash flow.

A good example of this is **PWR Holdings**, a recent addition to the portfolio. PWR listed on the ASX in November 2015 and designs and manufactures customised cooling systems for high performance automotive applications globally from its purpose built facility at Ormeau just south of Brisbane. The business has grown its revenue from $16.6m in FY13 to $32.5m in FY15 and expects revenue of nearly $50m in FY16. The business boasts high profit margins with pre-tax profit in FY13 of $3.9m growing to $11.9m in FY15 and expected to hit $14.9m this year. The business was established by Kees and Paul Weel in 1987 and between them they own 38.4% of the company and continue to run the business. PWR is a major provider of cooling systems for motorsports including an estimated 48% share of Formula One cooling products for the 2015 season. The company also supplies products to automotive OEMs and the automotive aftermarket, with future opportunities in emerging cooling technologies such as battery powered vehicles and energy capture and storage. We are optimistic about the prospects for PWR and have established an initial 2.5% position in the portfolio which will likely increase as we obtain more confidence in the management and business.

We look forward to reporting back to unitholders in the September update, on the performance of the underlying businesses in the Fund during the upcoming company reporting season. A distribution of 6.2666 cents per unit has been paid to unitholders on the register at June 30.