SANDON CAPITAL

Sandon Capital Activist Fund

December 2019 Monthly Report

Entry/Exit Prices: $1.7218/$1.7081

Performance Results (calculated net of all fees, assuming reinvestment of distributions and using unit mid-price. Indices are before fees.)

	1 month	1 year	3 yrs (p.a.)	5 yrs (p.a.)	Annualised since Fund inception	Annualised volatility since Fund inception	Total Return since Fund inception
SCAF	-1.4%	14.7%	7.1%	7.5%	11.5%	8.1%	207.2%
S&P/ASX 200 Accum.	-2.2%	23.4%	10.3%	9.0%	8.7%	11.5%	136.6%
Small Ordinaries Accum.	-0.3%	21.4%	10.0%	10.7%	5.1%	14.4%	66.7%

Net Monthly Returns

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2010	1.0%	-0.3%	-0.7%	2.9%	-4.2%	4.2%	4.4%	-0.6%	2.3%	2.4%	3.5%	-0.9%	**14.5%**
2011	1.3%	0.6%	0.5%	1.3%	-1.9%	-2.7%	-0.1%	-0.1%	1.9%	2.1%	2.5%	2.2%	**7.8%**
2012	-1.0%	0.4%	1.8%	2.1%	-2.8%	-1.0%	3.3%	0.5%	2.5%	2.8%	0.1%	2.2%	**11.1%**
2013	2.1%	3.2%	-1.4%	1.3%	2.8%	-3.7%	6.9%	0.7%	6.5%	5.7%	0.3%	0.3%	**27.1%**
2014	-0.3%	1.6%	1.9%	-0.3%	2.0%	0.5%	3.9%	2.1%	2.8%	-0.5%	1.0%	0.8%	**16.7%**
2015	-0.2%	0.0%	1.0%	0.3%	0.2%	-4.1%	3.9%	-4.9%	2.3%	3.5%	1.0%	0.9%	**3.6%**
2016	-1.3%	-3.3%	2.7%	1.8%	0.8%	0.7%	4.6%	0.0%	1.7%	1.5%	3.3%	0.1%	**13.1%**
2017	4.4%	-3.4%	0.2%	-2.0%	-1.3%	1.7%	1.3%	3.9%	-2.6%	0.2%	0.4%	2.9%	**5.5%**
2018	1.4%	-3.6%	2.2%	-0.2%	1.6%	3.1%	2.1%	3.0%	2.6%	-4.6%	-1.8%	-4.0%	**1.3%**
2019	0.2%	3.3%	1.0%	3.2%	2.7%	-2.3%	-0.2%	1.5%	4.9%	4.5%	-3.3%	-1.4%	**14.7%**

Portfolio Exposures

Net Exposure	95%	Long Positions	30
Net Cash	5%	Short Positions	3

Fund Commentary

The Fund return for December 2019 was -1.4%, bringing total returns (net of all fees and expenses) since inception to the equivalent of 11.5% per annum. Cash levels ended the month at approximately 5%.

City Chic Collective Ltd (CCX) was the largest detractor (-0.7%) this month, followed by Consolidated Operations Group (COG) (-0.6%). There was very little movement in other stocks in the portfolio.

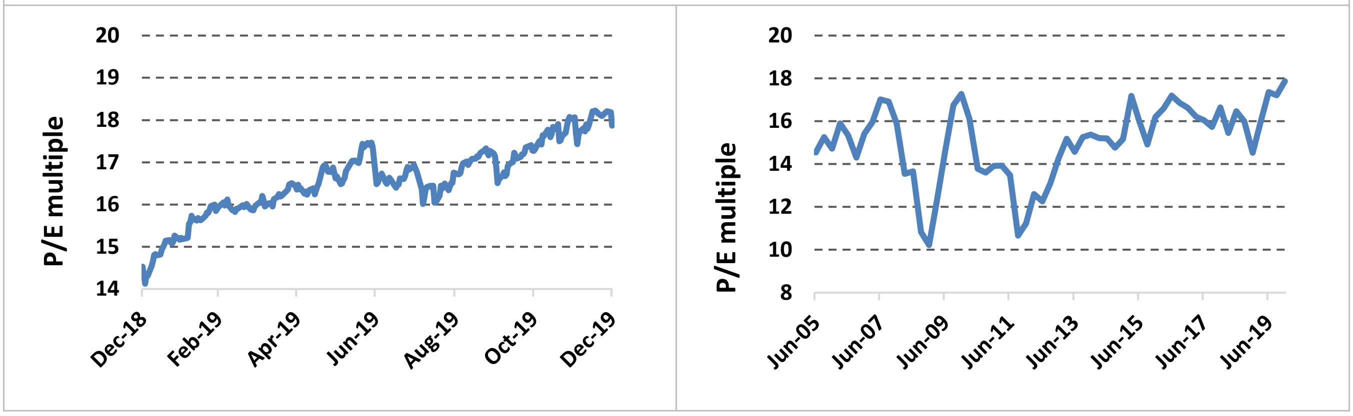
Calendar year 2019 was a strong one for the fund, generating a total return of 14.7%. However, this was less than market indices, which recovered strongly from the poor performance in 4QCY18 and also benefited from the increasingly higher prices that investors are willing to pay for earnings streams that at best are treading water, and in many cases are going backwards.

A recent research report from the Goldman Sachs Australian Strategy team highlighted the increasingly higher multiples that investors are willing to pay for listed equities. According to the report, which deconstructed the performance of stocks in Australia in CY19, 90% of the market's return came from Price-to-Earnings (P/E) multiple expansion, with the remainder of the return driven by dividends. Earnings downgrades, i.e. the fundamentals that will drive the longer-term share price performance of a company, were a headwind to the market's performance. At the end of November, the 12-month forward earnings per share estimates for the market as a whole, were 2% below where they started the year.

Looking forward, the Goldman report noted that following strong performance for equity markets driven by multiple expansion rather than strong fundamentals (i.e. earnings improvement), the return in the following year was generally poor. Whilst we don't try to predict the direction of equity markets, we remain wary that the multiples that investors are willing to pay for listed equities are at peak levels.

The chart below shows the 12-mth forward P/E multiple of the Australian market over the past 12 months (short term) and the past 15 years (long term). In an environment where equity markets are at peak valuations, we believe stock selection becomes very important to ensure precious capital is not put at risk.

12-mth forward P/E multiple of the S&P/ASX200 over the past 12 months (LHS) and 15 years (RHS)



Source: Bloomberg

Looking at the Fund's portfolio over the course of 2019 tells a different story to that of the market. As has been the case since inception over ten years ago, most of the portfolio's return was driven by company specific performance and events, rather than benefiting from the market's willingness to ascribe higher and higher valuations to companies that demonstrate no apparent improvement in underlying fundamentals. The five largest contributors to the Fund's performance in 2019 were City Chic Collective Ltd, OneMarket Ltd, Coventry Group Ltd, Spicer's Ltd and Iluka Resources Ltd.

City Chic Collective Ltd (CCX) had a very strong year with the share price improving 158%. In a very difficult retailing environment, the company reported 12.2% comparative sales growth in FY19, translating to underlying EBITDA growth of 25%. On top of the strong earnings growth, the solid balance sheet allowed the company to reinstate its dividend; the first time one had been paid in 5 years. In the last quarter of the year, CCX announced the acquisition of the e-commerce assets of Avenue Stores LLC (Avenue), a US-based specialty retailer targeting value-conscious women aged 25 to 55. If the management team, ably lead by Managing Director Phil Ryan, can successfully integrate the assets of Avenue and continue to grow its burgeoning US business, we expect the future for shareholders, including ourselves, to be very fruitful.

The fund first invested in OneMarket Ltd (OMN) in 2018, however substantially increased its position in late March 2019 when the share price plumbed all-time lows and was trading at less than half of net cash backing. At its AGM several months later, the OMN Chairman announced that the Board had *"been reviewing options to maximise value for shareholders and to proactively manage the discount to cash backing at which OneMarket trades."* This strategic review culminated in the company announcing that it would undertake an orderly winding-up and distribution of its assets. We commend the OMN Board for having taken this difficult decision. We expect to receive the bulk (>90%) of our current investment in OMN in the first quarter of 2020, with the remaining stub likely to be received in late 2021.

After many years of underperformance, Coventry Group Ltd (CYG) finally turned a corner in 2019. As a result of some judicious acquisitions and improving performance in the legacy businesses, the company returned to underlying profitability in FY19 with strong earnings and cash flow growth expected in FY20 and beyond. A strong balance sheet and highly cash generative operations provides significant capacity to make further bolt on acquisitions in fragmented industries. The company also has a bank of franking credits which should facilitate the resumption of dividends after a 5 year hiatus. The stock remains cheap (FCF yield >10%) and if management continues to deliver solid operational performance, we expect another strong year for CYG in 2020.

In early 2019, Spicer's Ltd (SRS) received a takeover offer from Japanese company, Kokusai Pulp & Paper Co., Ltd (KPP). The successful completion of the Scheme of Arrangement in July 2019, brought to an end a very rewarding investment in SRS, and its predecessor, PaperlinX. The Fund began accumulating a holding in the PaperlinX Preference Shares (PXUPA) in late 2015. In 2017, PXUPA were restructured by a conversion into ordinary SRS shares, thus waking the company from its pref-induced coma. Even after the restructure, SRS was largely overlooked by the market and traded at a substantial discount to its net assets until the KPP takeover offer. A new board nominated by shareholders, ably-led by Mr Jonathan Trollip, and the management team led by Mr David Martin, did an exceptional job leading the company to this opportunity.

After advocating publicly and privately for 3 years for Iluka Resources Ltd (ILU) to "spin-off" or demerge its valuable Mining Area C (MAC) Royalty, we were pleased to see the company announce a review of its corporate and capital structure in early November 2019. We believe the MAC Royalty is the best mining asset in Australia, and arguably the best single royalty anywhere in the world. Although ILU's review does not guarantee a demerger, the door is now well and truly open. We believe a demerger will lay the basis for what could, and should, become a globally significant royalty company.

Whilst 2019 was a very good year for equity markets globally, we expect the future to be more difficult. As a result of historically low interest rates, market participants are ascribing historically high multiples to equities, meaning further gains will be speculative rather than investment driven. Preservation of capital is our foremost objective, and in an environment where risk tolerance is high, it is more important than ever that we stick to our knitting and focus on idiosyncratic opportunities rather than relying on the market to drive returns. This should stand the Fund in good stead when the inevitable downturn in the market arrives.

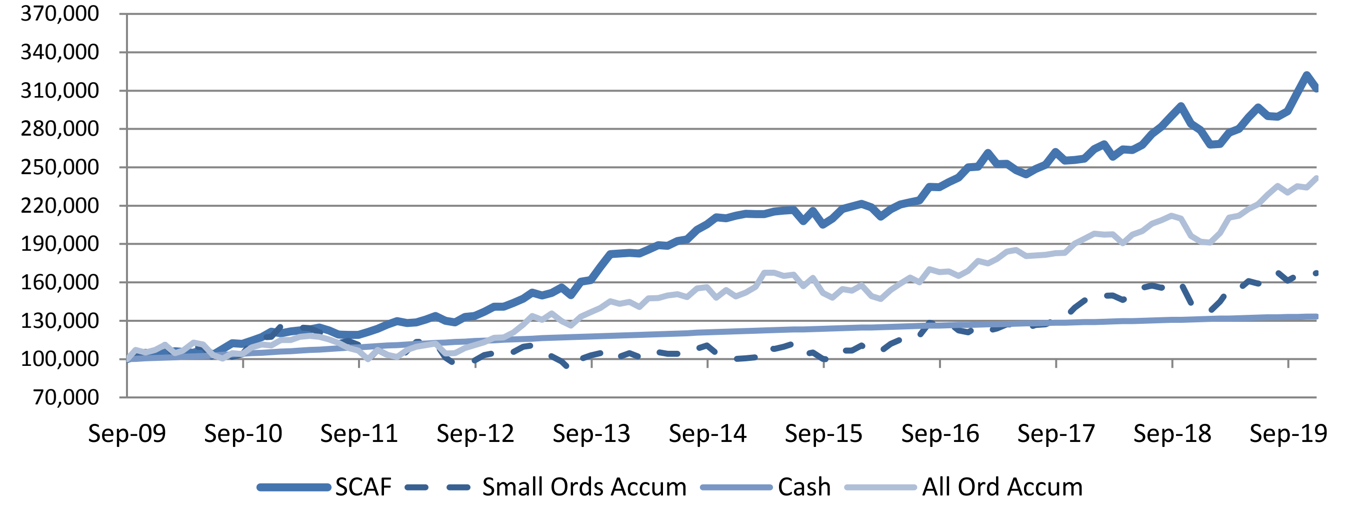
Fund Description

The objective of the Fund is to deliver returns to investors through a combination of capital growth and distributions. The Fund aims to achieve this objective by seeking to invest in opportunities that are considered by Sandon Capital to be trading below their intrinsic value and that offer the potential of being positively influenced by investors taking an active role in proposing changes in the areas of corporate governance, capital management, strategic and operational issues, management arrangements and other related activities. Neither returns nor capital are guaranteed.

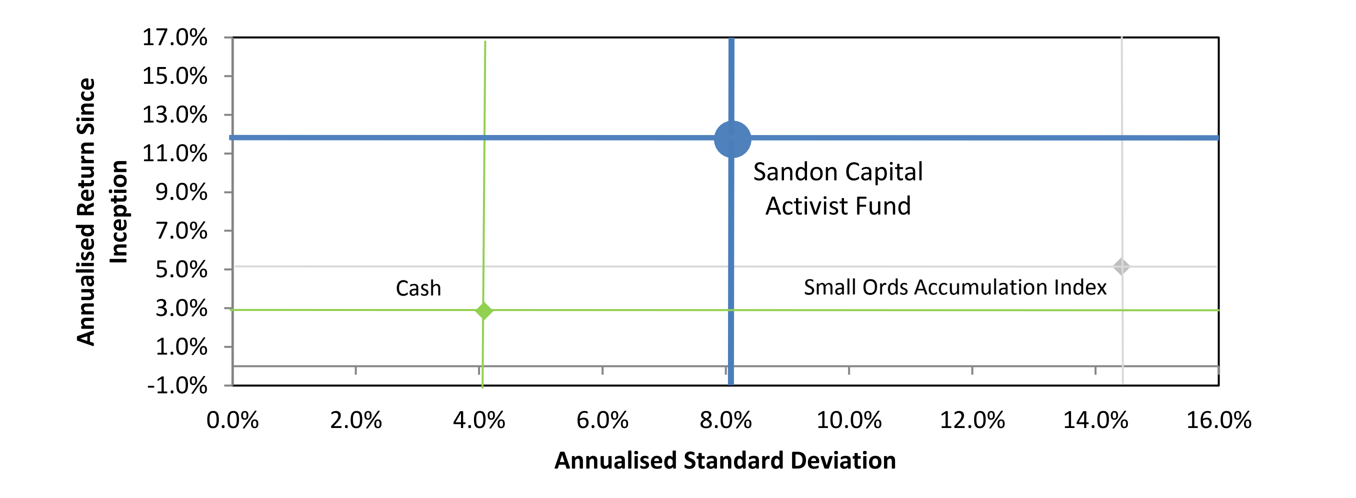
Fund Details

Structure	Wholesale unit trust	Minimum Investment	$250,000 (or as agreed with trustee)
Trustee	Fundhost Ltd	Trustee Fees	0.21%
Custodian	National Australia Bank	Management Fees	1.33%
Fund Auditor	EY	Performance Fees	15.375% of returns above cash
Investment Manager	Sandon Capital Pty Ltd	Highwater Mark	Yes
Website	www.sandoncapital.com.au	Buy/Sell Spread	±0.40%
Inception	4 Sep 2009	Applications/Withdrawals	Monthly/Quarterly

Growth of $100,000 invested since inception (assumes reinvestment of distributions)



Comparison of Annualised Return versus Volatility



Source for all charts: Sandon Capital, Bloomberg

Note: SCAF returns are net of all fees and expenses. Fund inception is 4 September 2009.