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Harness Asset Management Investment Report Dec 2015

Dear Investor,

Welcome to the Harness Asset Management Dec 2015 update.
When you have young kids the holiday season doesn't leave much time for rest and recuperation but at least it's a change and a chance to reflect on things from a different place.

During the recent week or so I have continued my reading of the wonderful "Poor Charlie's Almanac" about Warren Buffet's brilliant business partner, Charlie Munger. It is a book primarily about rational thought and wisdom. While being very interesting it's equally entertaining as Munger has that rare gift of imparting wisdom with a healthy dose of dry wit.

The other book that I'm trying to re-read during my break is "John Neff on investing" A more hands on portfolio management biography. Neff is one of the best long-term value investors ever. He ran the Windsor fund based in the US for over 30 years and out-performed the US market by over 3% p/a after fees over that time.

As many of you know, most fund managers never run a single fund for that length of time nor do they create that sort of consistent outperformance. I can recommend it as an educational read (although less entertaining than Munger) particularly those who are interested in running a portfolio in a fund management environment.

I have just completed my first year running the HAM Small Company's Value Fund. A combined anniversary and end of year seems a good time to reflect on performance and try to identify ways to improve.

The mistakes we have made have been great educational opportunities and we intend to take advantage of them and learn. The lack of portfolio management experience in the first year was evident and was the primary reason we didn't do better.

Being able to pick stocks doesn't automatically transfer into good portfolio management. Our performance was actually hindered by our largest positions. While they have not been disastrous they have impacted our short-term performance. Our largest position for example (FSA) was down slightly over the year while Arowana (AWN) dropped nearly 50%, United Overseas (UOS) was flat and Crown Notes (CWNHB) were surprisingly disappointing at the end of the year.

We had a number of stocks that performed well such as: Infigen (IFN) an 80% return, Ellex (ELX) which has delivered an unrealised gain of 111%, our unrealised gain in RFM Poultry (NSX:RFP) is now over 40% and Pacific Environment (PEH) delivered over 40% returns.

Despite these positives our large positions and a small number of poor investments have led to a flat year for the fund. We are significantly wiser around the issue of portfolio weightings and exploiting market momentum. We expect to execute more effectively in 2016.

Performance of founder's units to 30 Sept 2015:

Period	**Fund**	**ASX 300 Accumulation**
1 Month	**0%**	**2.7%**
3 Months	**-0.36%**	**6.53%**
6 Months	**-2.42%**	**-.35%**
1 Year	**0.4%**	**2.8%**
Since inception (Nov 2014) p/a	**1.03%**	**1.2%**
Size of fund	**$10m**	

Our portfolio

During the last quarter we liquidated our investment in CWNHBs. With speculation that James Packer was moving to privatise Crown and his resignation from the board, it seemed likely that we would be left owning a hybrid in an unlisted entity which appears hell bent on taking on the Casino World rather than maximising shareholder returns. The sale was disappointing but a reminder that almost anything can happen in markets.

PMP has been a significant investment for us during the year and while the company has delivered exactly what we anticipated, the stock has performed poorly. Despite PMP announcing an aggressive capital management strategy, there are just no value buyers left for it and it has fallen from recent highs. We have reduced our position.

The market's appetite for low growth value plays is very limited at the moment and while we would usually persevere we felt that a reduction of the position was prudent, particularly given the long term structural challenges of the industry. PMP now represents a break-even result, which is disappointing, as we have actually called the fundamentals well.

Another of our large positions, United Overseas Australia (UOS) has failed to move higher despite ever improving fundamentals. It has delivered a flat investment result so far yet we are well protected by asset backing and remain of the view that we will be rewarded for our patience eventually. The dividend pays us while we wait.

We have a number of stocks that are either under takeover or being wound up. These investments are expected to turn into cash in the quarter ahead leaving us with even more cash.

We are now sitting on 29 stocks and 23% cash which is more than I would like but I have been reminded this year that mistakes can be costly so we will wait for compelling opportunities. During this process we may underperform the market for a period of time but we will prioritise preservation of capital and be ready when we identify attractive risk/reward situations.

Please call me if you would like to discuss further.

Good investing and Happy New Year from the HAM team,

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