Suite 1102 Level 11
37 Bligh St
Sydney.
NSW, 2000.
Australia
Ph 04145858070

AFSL: 469551

Dear Investor,

Suspension of management Fee

While our 0.5% management fee is amongst the lowest in the market, we have decided to suspend it for at least 6 months during this period of weak performance. Harness Asset Management is well capitalised, the office rent is pre-paid for the year ahead and this will not compromise our capacity to operate in any way. We wanted to make a statement that recent performance was unsatisfactory to us and to show solidarity with our investors.

Having said all of that, we look at our portfolio and feel **it is pregnant with value and will ultimately reward us for our patience.**

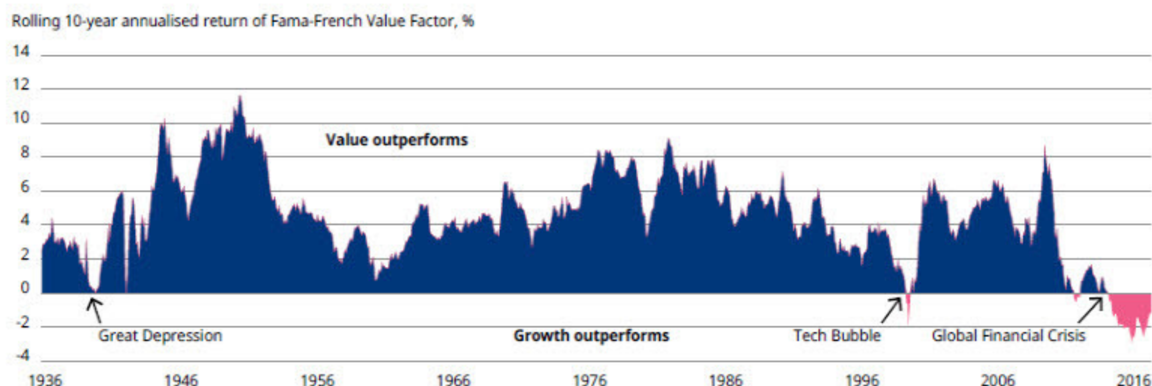
Our friends at Peters Macgregor sent us the following chart, which attempts to compare the difference in performance between growth investing and value investing.

While we are not sure about its predictive capacity, it is interesting that it is back to the same levels as 2000 just before the success of growth investing (during the dot com boom) came to an abrupt end.

The next chart recently published by Schroders shows how value investing has generally out performed growth over the long term apart from a small number of short periods. The exception has been the post GFC period. There are several reasons provided for this situation primarily the very slow economic growth recovery. Perhaps also the digital technology revolution has damaged the core earnings of so many traditionally cyclical stocks which would traditionally have been expected to see their earnings bounce back after an economic slowdown.

Either way, the incredible performance of growth stocks and continued expansion of earnings and revenue multiples cannot go on forever. Sanity will prevail.

Value has nearly always outperformed growth – until recently



Past performance is not a guide to future performance and may not be repeated.

Source: Kenneth French's Data Library and Schroders. Data from July 1926 to December 2017.

It's important (to us) after a period of weak performance, to consider explanations and make adjustments to our strategy if required. The ASX 200 Resource index was up around 30% for the 2018FY. Unfortunately, we have not had that resource stock exposure. In more recent times, we have built a uranium position. We own 4 Australian listed Uranium companies, which we believe provide a compelling risk/reward investment with significant upside for the risk. For those who did not catch our research report it can be see here uranium.

It is encouraging to see ongoing progress in the nuclear power industry. Last month, the UK government earmarked over $250m to support construction of new nuclear reactors. India signed a strategic cooperation agreement with GE for the planned construction of 6 reactors in the Maharashtra area in India. We also hear unofficial mumblings that Germany is reconsidering the rate at which it closes its 10 gigs of nuclear electricity generation. The great irony in Germany is that it spent huge amounts of money subsidising renewables (wind and solar) for years and the price of electricity is such now that its dispatchable electricity can't compete and is uneconomic and so is threatening the entire system and reliability of electricity. Germany currently relies on dirty brown coal (the biggest consumer of brown coal in Europe) and that infrastructure is ageing and new investment is not being made. Renewables are all well and good but they just don't work on a stand-alone basis due to their unreliable generation (IE they are wind and sun dependant). Combined with the expected growth in electric cars, electricity generation and grids need to accommodate some sort of dispatchable generation. We don't expect storage (batteries) will solve this issue in the foreseeable future. We will likely need to use Gas, Coal or Uranium for some time. It's a great shame that given how clean and safe Uranium is, that it has not been more widely adopted as core baseload power around the world and be used to compliment renewables. In the last few days, there has been more news coverage on the US investigation into its dependence on imported Uranium, particularly from Russian

friendly states. Commentators have suggested Trump will push for Tariffs on imported Uranium from some countries. This has led to a sound rally in the shares of Peninsula Energy (ASX:PEN), one of our holdings.

In the last month we have seen what we consider tax loss selling in some of our small caps that have had a tough year. This has compounded down trends during a time when buying is scarce. We expect a better quarter ahead but more importantly remain confident in the long-term performance of the fund. The natural volatility of small caps is generally high and we have missed a few opportunities to capitalise on this volatility by trading around our core positions. We will be working to exploit this volatility more effectively in future.

Please don't hesitate to contact us to discuss any potential investment in the fund.

Performance of founder's units to 30 Jun 2018 (net of fees):

Period	***Fund**	**ASX 300 Accumulation**	**Outperformance**
1 Month %	**0.33%**	3.19%	-2.85%
3 Months %	**-3.86%**	8.36%	-12.22%
6 Months %	**-7.26%**	4.27%	-11.53%
1 Year %	**3.65%**	13.24%	-9.59%
Since inception (Nov 2014) p/a *	**4.75%**	8.85%	-4.1%

Fund Size $13m *Assumes reinvestment of distributions. (No tax considered in providing figures)

Good investing,
Nigel Littlewood
20th July 2018

Note: Harness Asset Management Small Companies Value Fund (the Fund) own shares in the stocks mentioned above as at 30 Jun 2017. The above is in no way intended as financial advice, nor any recommendation by the manager of the fund.

This report has been prepared by Harness Asset Management Pty Ltd (ABN 61 158 314 982 AFSL 469551) and any views or commentary expressed herein are those of that party. This report contains general information only and has been prepared without taking into account your particular objectives, financial circumstances or needs. Before making any decision based on this report you should assess your own circumstances or consult a financial advisor. You should consider the Information Memorandum (IM) before deciding to acquire units in this fund. The IM is available at www.harnessam.com.au or contact us at admin@harnessam.com.au.
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