

AUSTRALIAN
RESEARCH
INDEPENDENT INVESTMENT RESEARCH

Cadence Opportunities Fund
(expected ASX code: CDO)

Pre-IPO Report

November 2018

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- 6) All staff are not allowed to trade in any stock or accept stock options before, during and after (for a period of 6 weeks) the research process.

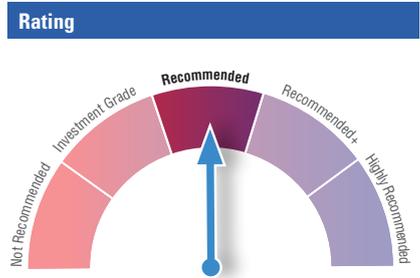
For more information regarding our services please refer to our website www.independentresearch.com.au.

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Note: This report is based on information provided in the Cadence Opportunities Fund Prospectus lodged with ASIC.



Key Investment Information	
Expected ASX Code	CDO
Offer Price (\$) per share	1.25
Expected Offer Close	30 November 2018
Expected Listing Date	20 December 2018
Min/Max Shares on Offer (m), not including oversubscriptions	13.2/80.0
Min/Max Capital Raised (m), not including oversubscriptions	\$16.5/\$100.0
Proforma NTA (\$) per Share (Min/Max Subscription)	1.25
Fees:	
Management Fee (p.a) ex GST	1.25%
Performance Fee	15.0%
Performance Hurdle	Previous high NTA

Key Exposure	
Underlying Exposure:	Portfolio of long and short positions in Australian and international securities.
FX Exposure:	The company will have direct foreign currency exposure in the event the Manager invests in international securities. The currency exposure will be hedged at the discretion of the Manager. Therefore movements in the currency exposure may impact the portfolio value in Australian dollars.

The investment opinion in this report is current as at the date of publication. Should circumstances of the issuer and/or product change, this may affect our investment opinion.

1. PRODUCT SUMMARY

Cadence Opportunities Fund (expected ASX code: CDO) is a newly created investment company that is seeking to list on the ASX and raise up to \$100m through the issue of up to 80m fully paid ordinary shares at \$1.25 per share. The company can accept oversubscriptions of up to \$100m. The company will provide exposure to an actively managed long/short portfolio, with a long bias, of Australian and international securities. Cadence Asset Management Pty Limited (Cadence or the Manager) has been appointed as the Manager of the portfolio. Cadence manages the portfolio of Cadence Capital Limited (ASX: CDM) using a similar investment philosophy and process that will be used for the CDO portfolio. The Manager uses a combination of fundamental and technical analysis in making investment decisions and has a disciplined entry and exit strategy. While the ideas generation process is based on the Portfolio Managers fundamental analysis and investment skill, the investment process is largely rules-based, with position sizing and timing all determined by technical rules. The portfolio is managed according to an open mandate, with no stock, sector or country limitations and, as such, is very much an alpha seeking mandate. CDO will focus on taking advantage of shorter-term duration trends with CDO effectively being a more active version of the CDM portfolio. The Manager will be paid an annual management fee of 1.25% p.a. of the portfolio value and will be eligible for a performance fee of 15.0% of the outperformance of the previous high water mark. The company may have direct foreign currency exposure in the event the Manager invests in international stocks. The currency exposure will be hedged at the discretion of the Manager. The Manager will be paying the costs of the offer. The company will provide a loan to the Manager to cover the costs of the offer, which will be repaid over 30 equal monthly instalments and will appear as an asset on the balance sheet. As such, the NTA will be the same as the offer price when the company commences trading.

2. INVESTOR SUITABILITY

An investment in the company is suitable for those investors seeking exposure to an actively managed, high conviction, long/short portfolio of securities. The company is expected to have a high level of turnover with the company seeking to take advantage of shorter-term duration trends. Therefore, investors should be comfortable with high levels of churn. The company will seek to pay regular fully franked dividends with the aim of steadily growing dividends over the long term. While the portfolio is expected to have a long bias, the Manager can short stocks. Investors should be comfortable with the additional risks associated with shorting stocks. The Manager will hold cash in the event investment opportunities cannot be identified. Reduced exposure to the market may result in the portfolio underperforming the market, however, will provide an element of capital protection in falling markets.

3. RECOMMENDATION

Independent Investment Research (IIR) has assigned Cadence Opportunities Fund (expected ASX code: CDO) a **Recommended** rating. The company will provide access to the Cadence investment philosophy, which has been proven to generate alpha over the last 15 years through the CDM portfolio. The Manager will be focusing on taking advantage of shorter-term duration trends in the CDO portfolio and will therefore be much more active than the CDM portfolio and will likely have a different return profile. The Manager has experienced a high level of turnover in recent times, with two of the three investment team members recently joining the Manager. However, we note that the newly appointed Portfolio Manager has a significant amount of experience in the funds management industry. Whilst new to the team, the new additions have both generated alpha in their short tenure with the Manager. The Manager is currently seeking to grow the investment team. The Manager has a disciplined investment process which lends itself to being repeatable and incorporates risk management with no more than 5% of the portfolio value (at cost) able to be invested in a single security. The strategy should lend itself to capital preservation in declining markets with the Manager moving to cash when the trend turns against the position. There is a lack of independent representation on the board, however, we note that the Managing Director of the Manager, Karl Siegling, will be making a significant personal investment in the company under the offer, aligning the interests of the Manager and shareholders.

4. SWOT

Strengths

- ◆ The Manager has a clearly defined investment philosophy and a robust and disciplined investment process. The rules based charter and processes employed lend themselves to a repeatable investment process and provides greater confidence that alpha generated can be attributed to both the process and individuals.
- ◆ There is a strong alignment of interest with shareholders, with the Managing Director and founder of the Manager, Karl Siegling, investing \$2m in the company under the offer.
- ◆ The Manager has a strong risk management process with the Manager entering positions in 0.5% increments in line with the trend, up to 5% of the portfolio at cost, and will scale out of positions in the event the trend reverses.
- ◆ The CDO portfolio will be managed using the same investment principles and a similar investment process that is used for the Cadence Capital Limited (ASX: CDM) portfolio, which was listed in December 2006 and has generated alpha in excess of the Australian market.
- ◆ The NTA will be the same as the offer price on the first day of trading with the Manager paying back the offer costs over 30 equal monthly instalments.

Weaknesses

- ◆ We do not view the performance hurdle of the high wark mark as appropriate.
- ◆ The company is newly established and while the portfolio will be managed using a similar investment strategy and process used to manage the CDM portfolio, this particular strategy has no performance history.
- ◆ The investment team is small with only three investment team members focusing on the portfolio and the investment team in its current state is relatively new with two of the three members of the investment team being with the Manager for less than 18 months. During their short tenure, the new additions to the team have both generated alpha to date. We note that whilst the two Portfolio Managers have not worked together for long, they both have a significant amount of experience in financial markets and funds management.

Opportunities

- ◆ The company provides investors access to a highly active, professionally managed long/short portfolio of domestic and international stocks.
- ◆ The company provides a more active version of the CDM portfolio with the Manager focusing on shorter-term duration trends, instead of just longer-term trends to take advantage of short-term volatility in the market. The investment strategy is designed to perform in both trending and sideways markets.

Threats

- ◆ The Manager has the ability to borrow up to 50% of the portfolio value to leverage its market exposure. The use of leverage can improve returns, however, can also magnify losses.
- ◆ Trend following investment strategies typically underperform in volatile market environments on account of what is referred to as 'whiplash'. High levels of volatility will likely see significant churn in the portfolio.
- ◆ The Manager can invest in international securities and as such may have direct foreign currency exposure. The currency exposure will be hedged at the discretion of the Manager. The portfolio value may be impacted, either positively or negatively, by movements in the relevant currencies.
- ◆ The Manager may short stocks. Shorting stocks entails a much higher degree of risk than a long position, given there is theoretically no limits to losses. We note that the manager has disciplined entry and exit rules that mitigate the short exposure risk to some extent.

5. STRUCTURE

PRODUCT OVERVIEW

Cadence Opportunities Fund (expected ASX code: CDO) is a newly created investment company that is seeking to list on the ASX and raise up to \$100m through the issue of up to 80m fully paid ordinary shares at \$1.25 per share. The company can accept oversubscriptions of up to \$100m. CDM shareholders will have a priority allocation of up to 60m shares in CDO (\$75m).

Cadence Asset Management Pty Limited (Cadence or the Manager) has been appointed as the Investment Manager of the portfolio. Cadence is a boutique fund manager that was established in 2003 and currently has ~\$415m in funds under management. The Manager intends to pay the costs associated with the offer. The company will loan the Manager the required amount and the Manager will repay the loan over 30 equal monthly instalments. No interest will be paid on the loan. The loan will appear as an asset on the balance sheet, allowing the NTA to be the same as the listing price when the company commences trading.

The company will provide exposure to an actively managed long/short portfolio, with a long bias, of both domestic and international securities using the Manager's investment process, which is based on a combination of fundamental and technical analysis. While the company can invest in both Australian and international securities, we expect the portfolio to be largely invested in Australian stocks, with the Manager historically having an average of 18% allocated to international securities through the CDM portfolio.

The portfolio will be concentrated given the investment universe with the portfolio holding up to 80 securities at any given time. The Manager may hold up to 100% cash if attractive opportunities cannot be identified. The portfolio will typically have a gross exposure less than 150%. The Manager can use debt to gear the portfolio, with the Manager able to borrow up to 50% of the portfolio value.

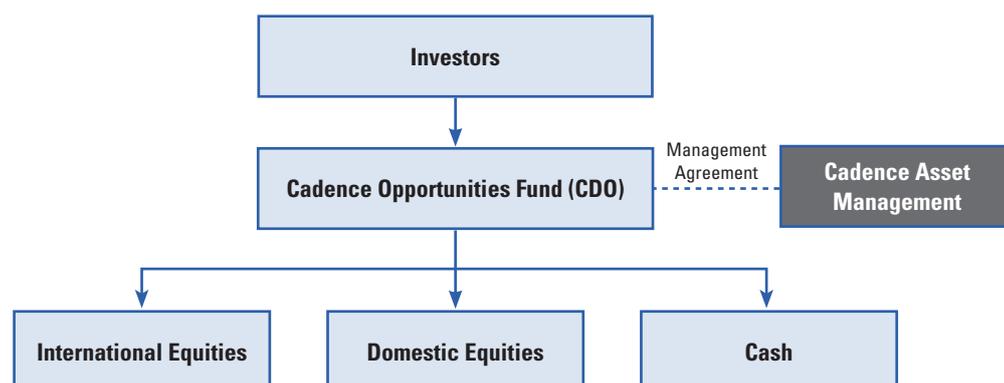
The Manager has a benchmark agnostic investment approach and an open mandate, with no sector or geographic limitations, however, the investment process ensures the Manager invests a maximum of 5% of the portfolio value, at cost, in a single security. The Manager does not have any limitations on the maximum exposure of a single position, therefore the Manager can let a stock price continue to move up (for long positions) or down (for short positions) until the exit signals are initiated. As such, strong performing stocks may account for a large portion of the portfolio.

The company may have direct foreign currency exposure in the event the Manager invests in international securities. The foreign currency exposure will be hedged at the discretion of the Manager. Therefore, movements in the relevant currencies may have an impact on the portfolio value in Australian dollars.

The company will seek to pay fully franked dividends from the trading gains and dividends received from the portfolio. The amount of the dividend will be determined by the board and will depend on several factors and be subject to prudent business practices. The company is expected to have a Dividend Reinvestment Plan (DRP).

The Manager will receive an annual management fee of 1.25% of the portfolio value and a performance fee of 15% of any outperformance over the previous high water mark.

INVESTMENT STRUCTURE



Product Leverage	
Used:	The Manager can use leverage in the form of debt to increase exposure to underlying securities. The Manager can borrow up to 50% of the portfolio value. The Manager can also short stocks which creates the effect of leverage. The portfolio will typically have a gross exposure less than 150%.
Capital Protection	na
Tax	
Disclaimer:	Tax consequences depend on individual circumstances. Investors must seek their own taxation advice. The following comments show Independent Investment Research's expectation of tax for ordinary Australian taxpayers, but cannot be considered tax advice.
Capital gains:	A capital gains tax (CGT) event will likely occur in the event the investor sells the shares on market for a higher price than it was purchased for. Investors will likely be eligible for the CGT discount if the shares are held for more than 12 months.
Dividends:	Dividends will likely be on income account in the year earned.
Legal Structure	
Wrapper:	Listed Investment Company
Investment Manager:	Cadence Asset Management Pty Limited
Investor Leverage	
Available:	No
Risks	The below is not a full list of all risks associated with the company but highlights what IIR considers to be the more significant risks associated with the company. A detailed risk assessment can be obtained from the Prospectus.
Short Selling Risk:	The company is expected to have a long bias, however, the Manager may short stocks. Shorting stocks entail a greater degree of risk than long positions as theoretically the loss could be unlimited.
Gearing Risk:	The Manager can borrow up to 50% of the portfolio value to leverage the market exposure of the portfolio. While leverage can magnify returns, it can also magnify losses.
Conflicts of Interest:	The board of the company is not expected to have a majority independent board. This means it would be unlikely for the Manager to be replaced irrespective of the performance of the portfolio. We note that the Managing Director of the Manager will have a significant personal investment in the company, aligning the interests of the Manager with shareholders.
Foreign Currency Risk:	The company may have direct foreign currency exposure in the event the Manager invests in international stocks. The currency exposure will be hedged at the discretion of the Manager. As such, movements in the relevant currencies may impact the portfolio value in Australian dollars, either positively or negatively.

6. MANAGEMENT & CORPORATE GOVERNANCE

BOARD OF DIRECTORS

The Board is expected to comprise of four members, two of which are expected to be independent and two of which are senior members of the Manager. The two independent directors have significant experience in their respective industries.

Board of Directors		
Name	Position	Experience
Karl Siegling	Non-Independent Director/ Managing Director	Mr. Siegling has 25 years investment experience in the financial sector both in Australia and overseas. Mr. Siegling holds a Bachelor of Commerce and a Law degree from the University of Melbourne and an MBA from INSEAD in France and a Post Graduate Diploma in Finance with the Securities Institute of Australia. Mr. Siegling commenced work in the Financial Services sector in Australia with Deutsche Morgan Grenfell, trading overnight currencies, bonds and bond options on the Sydney Futures Exchange. Mr. Siegling then worked within the Equities Research Division of Deutsche Morgan Grenfell before studying an MBA at INSEAD and working as a Summer Associate within the equities division of Goldman Sachs in London. Upon returning to Australia, Mr. Siegling was the Managing Director of eFinancial Capital Limited (a subsidiary of Challenger International Limited) focused on investing in early stage and expansion capital for financial services and technology companies. Mr. Siegling worked as a consultant for Wilson Asset Management, researching stocks, before setting up Cadence Asset Management Pty Limited. Mr. Siegling has been the Chairman and Managing Director of Cadence Asset Management Pty Limited (the Manager) for 15 and a half years and has been the Chairman and Managing Director of Cadence Capital Limited (ASX:CDM) for 15 years.

Board of Directors		
Wayne Davies	Non-Independent Director/ Chief Operating Officer	Mr. Davies has over 15 years funds management experience in Equity Long/Short Funds both in Australia and overseas. Mr. Davies is both a member of the South African Institute of Chartered Accountants and the Chartered Institute of Management Accountants. Mr. Davies is a founding member of the Cadence Asset Management team and has been the Chief Operating Officer of Cadence Asset Management for the past 10 years. Wayne Davies previously worked with Theorema Asset Management in London and was a director of Theorema Europe Fund and Theorema Europe Fund Plus
David Griffith	Independent Director	Mr. Griffith, B.E. (Hons) UNSW, is a chemical engineer and recently retired patent attorney. Mr. Griffith joined Spruson & Ferguson, Patent and Trade Mark attorneys in 1974 and became a Principal of Spruson & Ferguson 1981. He was the Managing Principal from 1999 to 2014. In 2014 he led the creation of IPH Limited which acquired Spruson & Ferguson and brought IPH to a successful IPO on the ASX in November 2014. Under his leadership, as the CEO and Managing Director, IPH Limited acquired a number of other intellectual property practices and was admitted to the S&P/ASX 200 in 2016. He was a Founding Director of Spruson & Ferguson Asia and was its Chairman from 2011 to 2017 when he retired from IPH. Mr. Griffith was an Australian delegate to the FICPI Executive Committee from 1983 to 1990 and he is a Member of Honour of FICPI. He was a representative partner to Computer Patent Annuities Limited Partnership (CPA) in Jersey, Channel Islands prior to his appointment to the Board from 2005 until it was sold to private equity in 2010. He is a past President and Fellow of IPTA (Institute of Patent and Trade Mark Attorneys of Australia), past President (Contact Commission) and Councillor of the Federation Internationale des Conseils en Propriete Industrielle (FICPI) from 1997 to 2012. He was an ex-officio member of the FICPI Advisory Council from 1997 to 2012. Mr. Griffith and his family entities have been a large shareholder of Cadence Capital (ASX:CDM) since its listing. His family entities also hold shares and units in a wide range of Australian and foreign unlisted and listed companies, LICs as well as unlisted funds, early stage seed investments and private equity investments.
Susan Oakes	Independent Director	Ms. Oakes has over 30 years financial services industry experience. Ms. Oakes has worked in trading room roles in Sydney, London and New York and is a former director and business head at Merrill Lynch. Ms. Oakes has also worked as a risk consultant at the Commonwealth Bank of Australia. Ms. Oakes has worked in trading roles at Genesis Proprietary Trading, Phoenix Trading Group, Aliom Holdings Limited & TransMarket Group and possesses extensive experience and knowledge in trading and portfolio management. Ms. Oakes holds a MBA from the Australian Graduate School of Management, UNSW, specialising in business risk.

INVESTMENT MANAGER

Cadence Asset Management Pty Limited (Cadence) has been appointed as the Investment Manager of the company's portfolio. Cadence is a boutique asset management company that was established in 2003. At the date of this report, the Manager had approximately \$415m funds under management.

The Manager is responsible for the management of the Cadence Capital Limited (ASX: CDM) portfolio. CDM was listed on the ASX in December 2006. CDM uses a similar investment strategy and process to that of CDO, with CDO effectively being a more active version of the CDM portfolio, with a focus on taking advantage of shorter-term duration trends. Since listing, CDM has delivered alpha compared to the ASX All Ordinaries Accumulation Index.

The investment team has experienced some turnover in recent times and in its current state is relatively new with two of the three investment team members only recently joining the Manager. The Manager is currently seeking to grow the investment team through the addition of a Portfolio Manager and a Sales Trader. Over their short tenure, the new additions to the team have produced alpha to date. Karl Siegling is ultimately responsible for the investment strategy and its implementation. Mr. Siegling founded the Manager in 2003 and has been investing using the Cadence investment philosophy and strategy since establishing the Manager. The alignment of interest with shareholders will be strong, with Mr. Siegling investing \$2m into the company via the offer.

The Investment Management Agreement (IMA) will be for an initial five years with an automatic extension for a further five years if the agreement hasn't been terminated earlier. The company will seek to obtain a waiver from the ASX to extend the initial period of the IMA to ten years.

Investment Team			
Name	Position	Years Experience	Years as part of the investment team
Karl Siegling	Managing Director and Portfolio Manager	25 years	15 years (founder)
Alan Crozier	Portfolio Manager	20+ years	>1 year
Charlie Gray	Equity Analyst	5 years	<1 year

7. INVESTMENT PROCESS

INVESTMENT OBJECTIVE

The company seeks to (1) achieve a high real rate of return, comprising both fully franked dividends and capital growth; and (2) provide investors with a co-investment opportunity alongside the Manager. The company seeks to achieve this using the Manager's disciplined investment process to invest in a long/short portfolio of Australian and international equities.

INVESTMENT PROCESS

- ◆ The Manager uses both fundamental and technical analysis in making investment decisions. It is the Manager's belief that the use of both fundamental and technical analysis has a greater probability of producing higher returns than either fundamental or technical analysis alone.
- ◆ Investments are classified as either trading or research driven core investments. The Manager will typically invest in up to 40 core investments and up to 40 trading opportunities in the portfolio at any point in time.
- ◆ Gross exposure of the portfolio will typically be less than 150%. Net exposure will generally be between 0% and 100%. The maximum leverage the Manager will employ via borrowings in the portfolio is 50%.

Idea Generation

- ◆ Ideas are generated from a number of sources including, the financial press, exchange announcements, company visits (proactive and reactive), speaking to brokers, company results, broker research, in-house research, macro views on specific sectors, amongst others. Where there is interest in a potential position these are then discussed by the investment team. Once an investment opportunity is identified it will undergo further analysis. A potential core investment requires both fundamental and technical analysis. A trading opportunity requires only technical analysis.
- ◆ Idea details are recorded and tracked in what is referred to as the Cadence Dashboard. This also provides an audit trail of all past ideas which can be followed up at points in time in the future when, for example, a stocks technical characteristics complement the fundamental characteristics.

Fundamental Analysis

- ◆ For core investments, fundamental analysis is undertaken. This may include discussions with management, industry research, and the generation of an in-house financial model for the potential investment. Following further investigation into a stock idea, a stock analysis sheet is completed for each potential core position - this sheet summarizes all the relevant fundamental and technical information. The analyst will then decide on whether the stock displays the characteristics of an ideal Cadence long position or short position. Most stocks analysed fall in the middle ground in that they do not display all the characteristics for either a long or a short position.
- ◆ The Manager looks to accumulate historical information and estimates for the next two years: EPS growth; P/E multiples; PEG multiples; operating cash flow and free cash flow yields per share; enterprise valuations; balance sheet strength, particularly debt and cash levels. Specifically the Manager is looking for stocks that meet the below tabled indicators.

Indicator	Long Position	Short Position
PEG	<1	2+
OCF Yield	12% - 15%	Negative - 8%
FCF Yield	8% - 10%	Negative - 3%
Cash	Yes	No
Debt	No	Yes

Technical Analysis

- ◆ The technical analysis component consists of the short term, medium term and long term share price and volume traded indicators, with a particular focus on shorter-term duration trends for this company.
- ◆ Essentially, the Manager is prevented from making a new investment, or increasing any existing position in any stock against the trend.

Portfolio Construction

- ◆ The Manager applies a disciplined entry and exit strategy to manage its portfolio holdings. Positions are scaled up following the trend. Positions are not entered against the trend.
- ◆ Ideas or positions have an initial 0.5% position of the portfolio at cost, with positions added to on a 0.5% basis up to a total exposure of 5% at cost as the stock price trend continues either up or down. The Manager follows the trend with respect to adding to a position. The net effect is that winning positions should account for an increasing proportion of the portfolio over time. The Manager does not add to losing positions or cut winning positions to maintain weightings in the portfolio. The process of entering and exiting individual stock positions defines the equity and cash exposure. Any stock exposure in excess of 5% is a result of capital growth in the stock.
- ◆ When divesting positions the positions are exited a third at a time. Once an initial sell signal is received, the Portfolio Manager assesses the fundamentals and trend of the stock to determine whether to initiate the sale process.
- ◆ The Manager will hold cash where attractive investment opportunities cannot be identified.

Investment Guidelines

Industry/Sector Limits	None
Geographic Exposure Limits	None
Position Size	Maximum position size will be no larger than 5% of the portfolio at cost.
Gearing	Maximum of 50% gearing
Net Exposure	Typically between 0% and 100% of the portfolio value.
Gross Exposure	Typically between 0% and 150% of the portfolio value.
Derivative Exposure	Derivatives exposure may not exceed 100% of the portfolio value.

8. PERFORMANCE ANALYTICS

SUMMARY OF ANALYTICAL RESULTS

CDO is a newly created investment company and as such has no performance history. We have provided the historical performance of Cadence Capital Limited (ASX: CDM) to provide insight into the Manager's portfolio management capabilities. We note that while the investment process is similar for both CDM and CDO, the management of CDO is expected to be much more active than that of CDM and therefore, the performance of the two portfolios are expected to have different return profiles.

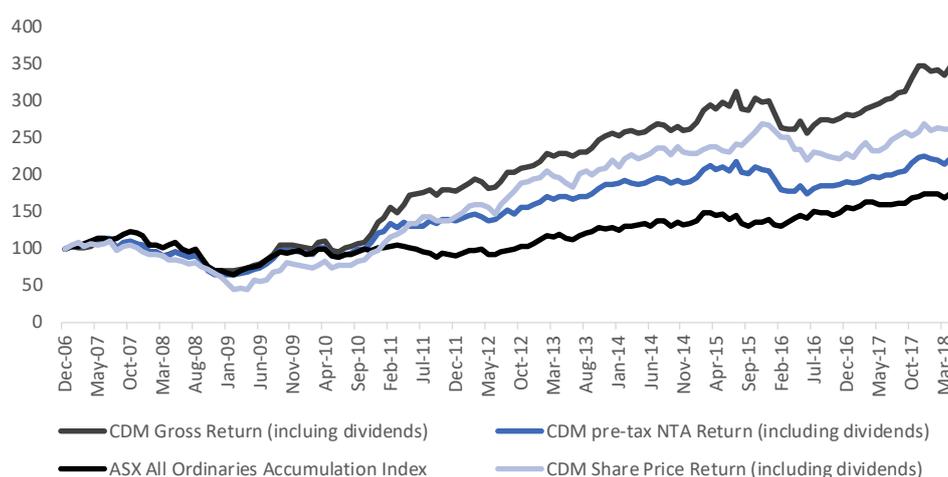
The key findings include:

- ◆ The CDM portfolio has outperformed the ASX All Ordinaries Accumulation Index (the market) since 31 December 2006 to 31 May 2018 on both a gross and pre-tax NTA basis. On a gross basis (before fees and expenses), the portfolio has returned 11.6%p.a over the period compared to the market return of 5.1%p.a. Taking into account fees, expenses and tax paid on realised gains (pre-tax NTA), the portfolio has returned 7.3%p.a.
- ◆ The CDM portfolio has experienced greater volatility than the market, yet has outperformed the market on a risk-adjusted basis on both a gross and pre-tax NTA basis since listing to 31 May 2018.
- ◆ The share price (including dividends) has outperformed both the pre-tax NTA and the market, returning 8.7%p.a. from 31 December 2006 to 31 May 2018.
- ◆ The portfolio has had a long bias with an average short exposure of 6.1% and an average long exposure of 82.8%.

PERFORMANCE HISTORY

- ◆ The below chart illustrates the historical performance of CDM's portfolio, both on a gross and pre-tax NTA basis, and share price (both including dividends) compared to the ASX All Ordinaries Accumulation Index (the market).
- ◆ The portfolio has significantly outperformed the market on a gross basis, with the portfolio returning 11.6%p.a compared to the market return of 5.1%p.a since 31 December 2006 to 31 May 2018. Gross returns do not include fees or expenses. On a pre-tax NTA basis (after fees, expenses and tax on realised gains), the portfolio has outperformed the market, returning 7.3%p.a. We note, the company listed in December 2006.
- ◆ Of note is the performance of investor returns (share price plus dividends). After performing worse than the pre-tax NTA and the market in the first few years of listing, the total share price return has outperformed both the pre-tax NTA and the market over the longer-term, returning 8.7%p.a. to 31 May 2018.
- ◆ The portfolio did not perform well during the GFC, a period in which it should have outperformed. This is largely due to the Manager hedging the exposure through the use of market futures. Given the structure of the portfolio this did not provide the desired protection. The Manager has stated that they will only enter short positions to generate alpha, not to hedge the market exposure, as such we would expect the Manager to outperform in the next severe downturn, as they would largely be holding cash. The Manager has significantly outperformed the market post the GFC.

CDM Historical Performance compared to the ASX All Ordinaries Accumulation Index



- ◆ The portfolio has performed well over both the short-and-long term. Given the concentration of the CDM portfolio and the investment approach of the Manager, there will be periods of outperformance and underperformance, as is highlighted by the below table. For example, over the 12 months to 31 May 2018, the pre-tax NTA (including dividends) has outperformed the market, however, has underperformed over the three year period to 31 May 2018. The average annual rolling return for the CDM pre-tax NTA (including dividends) since listing to 31 May 2018 is 8.8% and 13.7% on a gross basis, compared to 5.5% for the market. This suggests that the Manager has been able to generate alpha consistently over the long-term.
- ◆ On a risk-adjusted basis, CDM has outperformed the market since listing to 31 May 2018, with a sharpe ratio of 0.32 for the CDM portfolio on a pre-tax NTA basis compared to a sharpe ratio of 0.17 for the market. The heightened volatility of the CDM portfolio has been more than offset by the improved returns over the market.

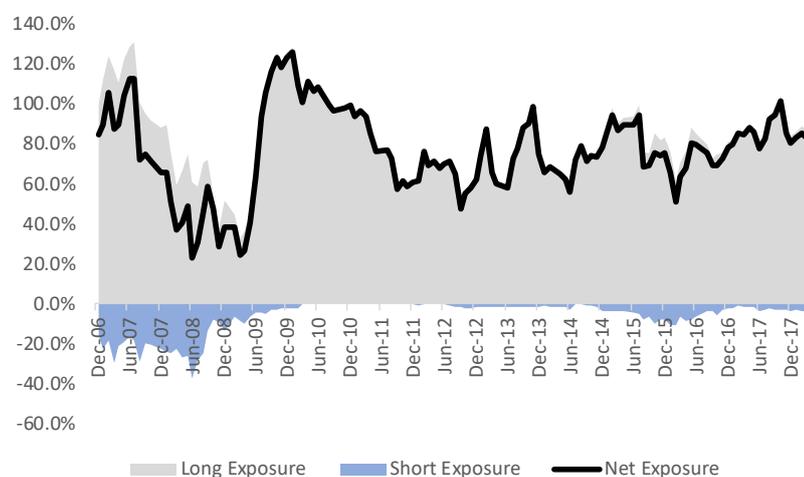
Historical Performance (31 December 2006 to 31 May 2018)

	CDM Gross Returns (including dividends)	CDM pre-tax NTA Return (including dividends)	ASX All Ordinaries Accumulation Index	CDM Share Price Return (including dividends)
Returns:				
1 year	19.0%	14.8%	10.8%	12.0%
3 year (p.a)	5.6%	2.2%	6.4%	4.0%
5 year (p.a)	14.2%	10.3%	13.9%	11.0%
10 year (p.a)	13.9%	9.0%	5.1%	11.8%
Since Listing (p.a)	11.6%	7.3%	5.1%	8.7%
Average Rolling Annual	13.7%	8.8%	5.5%	12.6%
Risk:				
Volatility	14.7%	14.5%	13.8%	19.0%
Sharpe Ratio*	0.60	0.32	0.17	0.32
Upside Capture Ratio	0.84	0.77	-	-
Downside Capture Ratio	0.44	0.58	-	-

*Calculated using the 10 year Australian government bond rate of 2.70% at 31 May 2018.

CDM Historical Exposure

- ◆ The CDM portfolio can invest both long and short, however, has had a long bias with an average long exposure of 82.8% and an average net exposure of 76.8% from listing in December 2006 to May 2018. We expect the portfolio exposure of CDO to be similar.
- ◆ The Manager has the ability to borrow to leverage its positions. The Manager has used leverage to gain additional exposure to the market, with a maximum net long exposure of 126.1%.
- ◆ Since listing, CDM's portfolio has had an average cash holding of 23.2%, with a maximum cash holding of 76.7% in June 2008.

Historical Exposure**9. PEER COMPARISON**

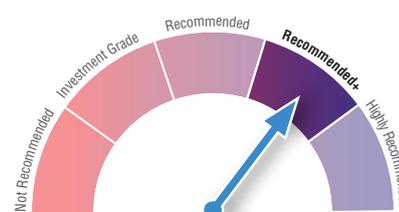
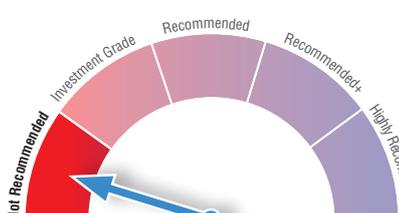
- ◆ We have provided a comparison of some of the key features of the company with other LICs that have predominantly Australian exposure with the ability to invest internationally and two recent listings that provide global exposure. We note that the below includes LICs that have a long only mandate and a long/short mandate, however, those LICs with a long/short mandate all have a long bias.
- ◆ The annual management fees being paid by the company are on the high side at 1.25%p.a. compared to its peers. The performance fees are at the low end of those companies that charge performance fees, however, the performance fees of all but one of the other LICs are paid based on the outperformance of a market index. The company will pay performance fees on the outperformance of the previous high water mark. We do not view this performance hurdle as appropriate.

Peer Comparison						
LIC Name	ASX Code	Listing Date	Strategy	Management Fee (%p.a, ex GST)	Performance Fee (%)	Performance Fee Hurdle
Clime Capital Limited	CAM	February 2004	Long only	1.0	20.0	ASX All Ordinaries Accumulation Index or the increase in the portfolio value if the market has declined
Cadence Capital Limited	CDM	December 2006	Long/Short	1.0	20.0	ASX All Ordinaries Accumulation Index
Contrarian Value Fund	CVF	January 2015	Long/Short	1.0	20.0	S&P/ASX 200 Accumulation Index or the increase in the portfolio value if the market has declined
Perpetual Investment Company	PIC	December 2014	Long only	1.0	na	-
VGI Partners Global Investments Limited	VG1	September 2017	Long/Short	1.5	15.0	High Water Mark
WAM Global Limited	WGB	June 2018	Long/Short	1.25	20.0	MSCI World Index Net, AUD
Cadence Opportunities Fund	CDO	-	Long/Short	1.25	15.0	High Water Mark

APPENDIX A – RATINGS PROCESS

INDEPENDENT INVESTMENT RESEARCH PTY LTD “IIR” RATING SYSTEM.

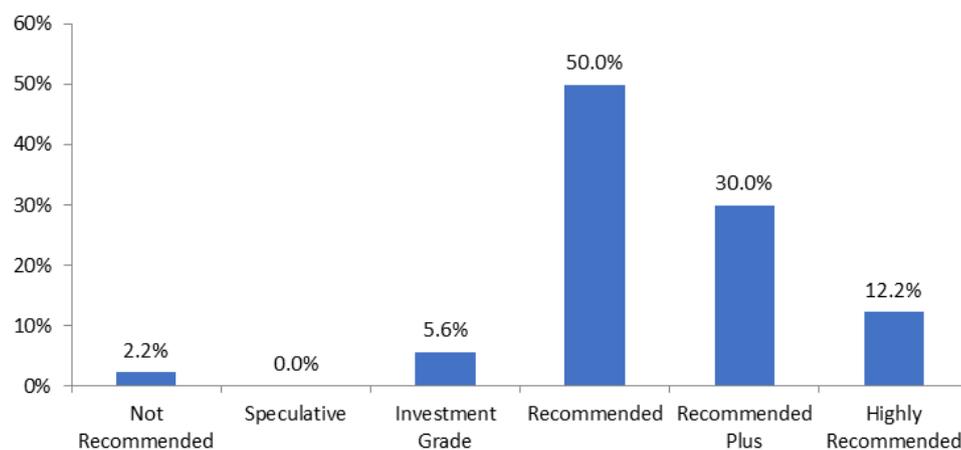
IIR has developed a framework for rating investment product offerings in Australia. Our review process gives consideration to a broad number of qualitative and quantitative factors. Essentially, the evaluation process includes the following key factors: product management and underlying portfolio construction; investment management, product structure, risk management, experience and performance; fees, risks and likely outcomes.

LMI Ratings	SCORE
<p>Highly Recommended</p> 	<p>83 and above</p> <p>This is the highest rating provided by IIR, indicating this is a best of breed product that has exceeded the requirements of our review process across a number of key evaluation parameters and achieved exceptionally high scores in a number of categories. The product provides a highly attractive risk/return trade-off. The Fund is likely effectively to apply industry best practice to manage endogenous risk factors, and, to the extent that it can, exogenous risk factors.</p>
<p>Recommended +</p> 	<p>79–83</p> <p>This rating indicates that IIR believes this is a superior grade product that has exceeded the requirements of our review process across a number of key evaluation parameters and achieved high scores in a number of categories. In addition, the product rates highly on one or two attributes in our key criteria. It has an above-average risk/return trade-off and should be able consistently to generate above average risk-adjusted returns in line with stated investment objectives. The Fund should be in a position effectively to manage endogenous risk factors, and, to the extent that it can, exogenous risk factors. This should result in returns that reflect the expected level of risk.</p>
<p>Recommended</p> 	<p>70–79</p> <p>This rating indicates that IIR believes this is an above-average grade product that has exceeded the minimum requirements of our review process across a number of key evaluation parameters. It has an above-average risk/return trade-off and should be able to consistently generate above-average risk adjusted returns in line with stated investment objectives.</p>
<p>Investment Grade</p> 	<p>60-70</p> <p>This rating indicates that IIR believes this is an average grade product that has exceeded the minimum requirements of our review process across a number of key evaluation parameters. It has an average risk/return trade-off and should be able to consistently generate average risk adjusted returns in line with stated investment objectives.</p>
<p>Not Recommended</p> 	<p><60</p> <p>This rating indicates that IIR believes that despite the product’s merits and attributes, it has failed to meet the minimum aggregate requirements of our review process across a number of key evaluation parameters. While this is a product below the minimum rating to be considered Investment Grade, this does not mean the product is without merit. Funds in this category are considered to be susceptible to high risks that are not reflected by the projected return. Performance volatility, particularly on the down-side, is likely.</p>

APPENDIX B – MANAGED INVESTMENTS COVERAGE

The below graphic details the spread of ratings for managed investments rated by Independent Investment Research (IIR). The managed investments represented below include listed and unlisted managed funds, fund of funds, exchange traded funds and model portfolios.

Spread of Managed Investment Ratings



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