HARRINGTON PARTNERS

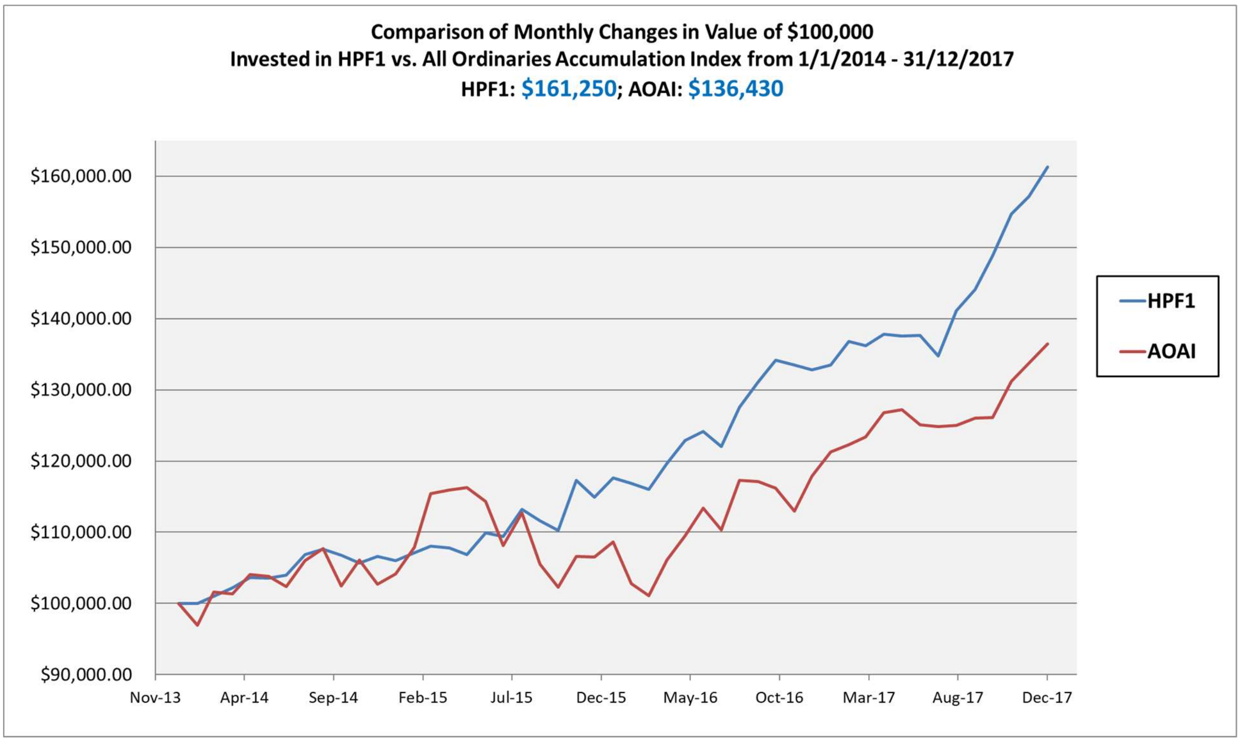
Investment Management

Harrington Partners Fund 1 HY18 Investor Letter

Harrington Partners primary goal is to protect investors capital and outperform the Australian All Ordinaries Accumulation Index (AOAI) by 3-5% annually as measured over rolling 5-year periods. The Fund managers have the majority of their investable assets in the Fund, this creates a very strong alignment of interests between the managers and investors with a concentration on achieving the highest possible risk adjusted returns.

	HPF1 Net Return*	AOAI Return#	Relative Performance
6 Months to 30/06/2014	3.71%	2.36%	1.35%
30/06/2015	5.51%	5.67%	-0.16%
30/06/2016	11.50%	2.01%	9.49%
30/06/2017	10.48%	13.12%	-2.64%
6 Months to 31/12/2017	19.63%	9.31%	10.32%
Annualised Performance	12.69%	8.08%	4.61%
Cumulative Performance	61.25%	36.43%	24.82%

#Data source for AOAI Returns: S & P Dow Jones Indices LLC. *Net Return to investors which is less fees and charges but includes reinvested distributions. Past returns are not a good indication of future returns.



Harrington Partners Fund 1 (HPF1, the Fund) finished the Half Year 2018 (HY18) with a unit price of **$1.5402**, equating to a gross return of **24.18%** (before accounting for fees). The Fund does not try to match any index or benchmark; however, it is necessary to test performance against a pre-determined and relevant reference point. For this purpose, the All Ordinaries Accumulation Index (AOAI) is suitable given it includes reinvested dividends and provides a relevant comparison to what an investor could achieve in a low-cost broad-based index fund. Over the past 6 months an investment in the AOAI would have returned 9.31%. With distributions reinvested and net of all fees, HPF1 has returned **61.25%** since inception, as against a return for the AOAI of 36.43% over the same period.

The Harrington Partners Approach

Harrington Partners' primary objective is to protect investors capital whilst achieving performance that is superior to the market average over the medium to long term. We are patient value orientated investors with a fundamental approach that is thorough, creative and flexible. Our investment universe is not pre-determined by size, industry, or geography, providing us with the ability to operate in areas that are out of favour or not as widely researched by the broader investment community.

We do not follow any rigid formulas or complex rules and avoid the need for overly optimistic long term predictions, complex financial products, or elaborate modeling. We do not trade price movement, trends, or macro-economic theories.

Our process has a core emphasis on minimising error. We proactively work to mitigate the possible impacts of psychological and cognitive biases on our decision making and have intentionally built an operating structure that supports this.

We see ourselves as business owners and although the bulk of what we do is numbers driven, we focus intently on both the tangible and intangible qualitative elements which are necessary for a successful investment. We view the management teams of the businesses in which we invest as our partners and therefore demand high levels of integrity, skill and alignment with shareholder interests.

Our first preference is to pay sensible prices for well managed businesses that are conservatively financed, possess durable competitive advantages and have the ability to grow their franchise over time. Opportunities to buy these businesses at prices below our appraised intrinsic value are rare. When we do find opportunities that meet these criteria, we are willing to own them indefinitely, provided that the fundamental investment hypothesis remains sound.

If our first preference cannot be met, we are committed to scouring the market in search of situations where the probabilities of achieving superior returns are in our favour.

Resources are concentrated on our best investment ideas; this has the potential to lead to volatility relative to the market average. We do not consider this type of volatility to be a relevant measure of risk for the long term investor. Rather, our primary determinant of risk is the probability of permanent loss of capital. Ultimately, if we are unable to find opportunities that meet our investment criteria, then we hold cash.

We only get paid for positive performance and the majority of our investable net worth is in the Fund, thus ensuring a strong alignment of interests with partners. Investing is our passion and we continually strive for improvement, both professionally and personally.

Our goal is to establish mutually beneficial long term relationships with partners who align with this philosophy and appreciate that meaningful wealth creation requires time and persistence. Achieving our economic objectives is crucial to HPF1s enduring success. However, building a business that all partners are proud to be part of, and appreciating the journey, are equally important.

The Portfolio

Portfolio Weighted Average Market Capitalisation	$177 million
Number of companies	22
Australian Shares	70%
International Shares	1%
Cash	29%
Concentration of top 5 holdings	62%*

*Of invested capital

The Fund owns shares in 22 companies with 62% of capital invested concentrated in the 5 largest holdings. The top 10 holdings made up 60% of the total portfolio. Cash weighting is 29% of the portfolio and is now much closer to our long term intentions for cash weighting compared to the weighting of 58% at the end of FY17.

The Fund has had the strongest 6 months since inception for the first half of financial year 2018. We stated at the end of FY17 that “Our view is that there is a significant amount of unrealised value within the current portfolio” and this value has largely become realised over the period, we are confident there is still a meaningful amount of unrealised value in the portfolio but the returns of the past 6 months should not be expected over the coming 6 months. The returns are a consequence of the investment decisions made in previous years and it is welcoming to see some of our larger positions coming to fruition.

The top 10 holdings at December 31, 2017 were:

Rank	Holding	Total Portfolio Weighting	Total Equity Weighting
1	Boom Logistics (ASX:BOL)	15.86%	22.34%
2	Undisclosed	8.80%	12.40%
3	Macmahon Holdings (ASX:MAH)	8.62%	12.15%
4	Undisclosed	5.30%	7.47%
5	Fleetwood Corporation (ASX:FWD)	5.14%	7.24%
6	Undisclosed	4.84%	6.82%
7	Undisclosed	4.69%	6.60%
8	FSA Group (ASX:FSA)	2.81%	3.96%
9	Undisclosed	1.91%	2.69%
10	United Overseas Australia (ASX:UOS)	1.91%	2.68%

We have disclosed 3 new top 10 positions as these companies are established positions which the Fund is no longer actively buying at current prices. Further top 10 positions will be disclosed as they become established.

We have added seven new companies to the portfolio over the first half of FY18, 3 of which are now in our top 10 holdings (all undisclosed). Although we do not expect a repeat of the returns over the last 6 months, we believe the probabilities are in our favour that these new positions should help to underpin meaningful returns for the Fund over the next 2-3years. With the cash weighting of the Fund decreasing the hurdle rate for any new potential investment becomes higher. We are not concerned with short term price fluctuations and as always would welcome any pull back in the broader market that would give us the opportunity to potentially add new positions or increase the size of our current positions at lower prices. It can be unnerving to watch the market value of your investments decrease, especially when, as is usually the case, this happens quickly. However, this scenario is ideal for long term investors in productive assets as it usually gives the chance to purchase these assets from a seller who is forced to sell and/or not making a rational judgement on underlying value.

Cryptocurrencies is an area that we keep being asked about over the past 6 months. Many people have made substantial gains from speculating in 'cryptos' over the past 12 months, the Fund however has not been a participant. We may miss out on potential profits from this area of the market, but we are not willing to venture outside of our circle of competence for what we see as mainly a fear of missing out from most participants. We will remain disciplined to our investing philosophy and process and believe this will provide the largest returns over time.

The appendix to this letter contains an extended discussion on our largest investment in Boom Logistics [ASX:BOL].

We are privileged that you have chosen to partner with us on this journey. As always, we welcome any feedback and if you have any questions, comments or investment ideas please do not hesitate to contact us.

Yours Sincerely,

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APPENDIX

Boom Logistics [ASX: BOL]

BOL is an industrial services company with national coverage that provides complete heavy lifting solutions, along with external crane and travel tower hire, to the resources, energy, utilities, and infrastructure sectors. The business wholly owns it modern fleet of cranes and travel towers and employs an experienced workforce of lifting professionals. BOL is currently the Funds largest position being 15.86% of the current portfolio and is also one of the longest held positions with an initial investment being made nearly four years ago.

In simple terms, our original thesis was that BOL was being sold at a very attractive discount to its productive net tangible assets (NTA) and represented good value for a patient investor willing to ride out the inevitable cyclicality of its operations. In early 2014 when the Fund first invested BOL was, justifiably, very unpopular and shares could be bought for $0.15 against a per-share NTA of $0.51. The business's main revenue source was from the resources industry, specifically Western Australia, which was in the midst of a deep downturn. During the boom years that preceded the downturn BOL had assumed an imprudent level of financial and operational leverage and this left them vulnerable as revenue dried up across the industry.

The business was faced with the challenging task of managing a significant deterioration in cash flow and asset values whilst trying to meet its substantial interest and debt covenant liabilities. Management enacted a strategy of widespread asset sales in the hope it would provide the necessary cash flow to meet debt obligations and ultimately avoid insolvency. However, the industry wide downturn meant the market was being flooded with comparable assets and eventual sale prices proved to be at deep discounts to prevailing book value. We expected this process to be painful, however we were satisfied that the probabilities were in our favour that BOL would be able to stay in business, meet its liabilities, and ultimately emerge with a valuable fleet of assets capable of taking advantage of a cyclical recovery without the need for excessive capital expenditure.

Between FY14 and FY17 revenue and NTA value declined by over 44% and 40% respectively, whilst the share price basically halved and reached a low of $0.063 in mid-2016. During this time, we continued to research the business and had multiple meetings with management which increased our conviction that the right things were being done to address the near-term issues whilst maintaining longer-term value. We backed this perspective with ongoing share purchases and, as at 30 Dec 2017, the Funds average buy price was $0.108 per share.

Fortunately for BOL, activity in the resources industry has started to recover and the business is experiencing strong demand from the current resurgence in infrastructure spending along with their market leading position in wind farm construction. Concurrently, management has been successful at substantially reducing debt, lowering the cost of doing business, and maintaining a fleet capacity that is now able to take advantage of the improvement in market conditions. The combination of these factors has enabled a stabilisation of revenue and operating margins to a point where we now expect BOL will be able to benefit from substantial near-term operating leverage. The market has rewarded this change of fortune with the share price now trading at $0.245[1]. HPF1s investment in BOL remains ongoing as we believe the business still represents good value despite the fact that a substantial proportion of our original thesis has now run its course. We will continue to provide updates on Boom as time progresses and the investment is, as always, being monitored very closely.

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[1] As at the time of writing

DISCLOSURES: