

HARRINGTON PARTNERS

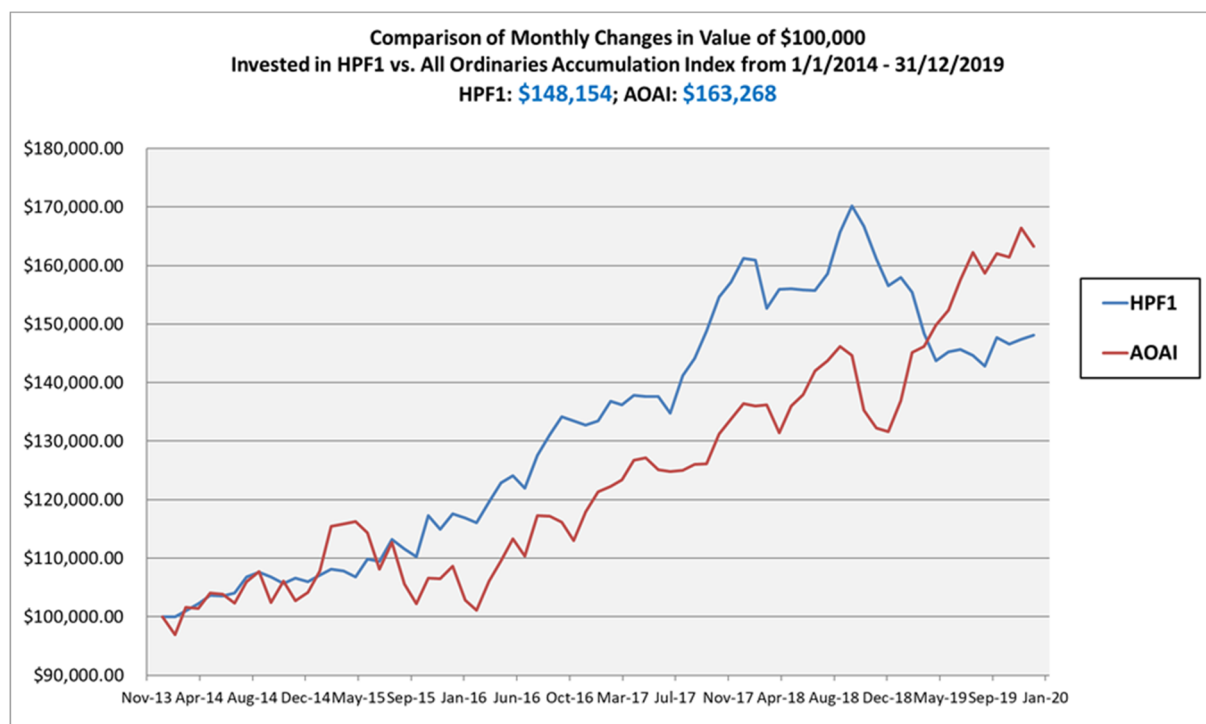
Investment Management

Harrington Partners Fund 1 (HPF1) – 31 December 2019

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%
30/06/2018	15.49%	13.73%	1.76%
30/06/2019	-6.45%	11.04%	-17.49%
6 Months to 31/12/2019	1.71%	3.59%	-1.88%
Annualised Performance	6.77%	8.51%	-1.75%
Cumulative Performance	48.12%	63.28%	-15.16%

#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.



The Fund returned 1.71% net to investors during the first six months of Financial Year 2020 (FY20), this compares to a return of 3.59% for the AOAI over the same period.

The top 10 holdings at December 31, 2019 were:

Rank	Holding	Total Equity Weighting	Total Portfolio Weighting
1	Locailty Planning Energy (ASX:LPE)	16.59%	8.57%
2	EVZ Limited (ASX:EVZ)	15.52%	8.02%
3	Enevis Limited (ASX:ENE)	14.33%	7.40%
4	United Overseas Australia (ASX:UOS)	11.45%	5.91%
5	Kangaroo Island Plantations (ASX:KPT)	11.25%	5.81%
6	Blackwall Limited (ASX:BWF)	7.37%	3.81%
7	Blackwall Property Trust (ASX:BWR)	7.11%	3.67%
8	FSA Group (ASX:FSA)	6.57%	3.40%
9	Gowing Brothers (ASX:GOW)	6.20%	3.20%
10	Berkshire Hathaway (NYSE:BRK B)	1.35%	0.70%

The top ten holdings made up 50.5% of the total portfolio with the largest change over the period being the increased cash weighting from 38% to 48%.

Specific changes within the equity component include the sale of **Fleetwood Corporation [ASX: FWD]** and a smaller holding in **Excelsior Capital [ASX: ECL]** both of which have been held by the Fund for over four and a half years. These businesses had several characteristics which made them unsuitable for longer-term investment with the most prominent being the absence of management teams with the characteristics we require. There will be further changes to the portfolio throughout FY20.

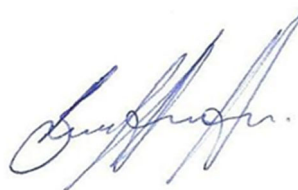
Kangaroo Island Plantations [ASX: KPT] has unfortunately been in a trading suspension since the last days of December as the company assesses the longer-run impacts of bushfires which severely damaged over 95% of their timber crop. Insurance pay-outs are likely to only cover around half the standing value of the timber as the scale of loss is well beyond their maximum annual claims limit. This outcome significantly changes the operating dynamic and investment value of KPT as the expected timing of positive cashflows has been pushed much further into the future. There is still potential for value to be realised but at this stage we do not expect KPT to come back to the market for several months and when it does it is likely to trade at a lower price.

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 (Business Discussion)

BlackWall Limited [ASX: BWF] is a commercial property investor and manager with formative roots dating back over 25 years to a company that was co-founded by the current Chairman and largest shareholder Seph Glew.¹ BWF generates management, performance and transaction fees for managing third party real estate investment structures, with the largest of these being from their management of the **BlackWall Property Trust [ASX: BWR]**². The company's business model is inherently capital-light and scaleable and driven by an operating philosophy that is best described as being patient, persistent, and opportunistic.

*"BlackWall's property development, management and funds activities are essentially the same as they have been for over 25 years. We look for assets that have a problem that we think we understand and can fix. We look at real estate that is suitable for adaptive reuse and urban renewal at a price that mitigates, at least in part, the risks associated with changes of use... More often than not, the best opportunities present when investors and institutions are least likely to invest. Our strategy requires patience but can generate material value gains and sustainable income especially during periods of dislocation in financial markets."*³

Board members Seph Glew, Robin Tedder, Stuart Brown, and Richard Hill have together built an exceptional multi-decade record of shrewd investment and operating judgement, and they collectively own around 37.5% of BWF. They have navigated several 'battle-hardening' experiences such as the 1987 stock market crash, the early 1990's commercial property collapse, and the global financial crisis. As a result, these leaders have instilled a pragmatic ethos that primarily seeks to exploit the cyclical nature of the markets they inhabit. As an example, the following messages were delivered at the company's 2008 AGM during the midst of the GFC:

"I am sure it is apparent to everyone in this room and to all of our shareholders that we are entering an entirely new financial world. The excesses that are being uncovered in the current meltdown already exceed those exposed following the 1987 share market crash and we expect the aftermath of this correction to be significantly greater. I, and several of my fellow directors, experienced first-hand the effects of the 1987 share market crash and we made this a feature of our staff get-together in August 2007. By the beginning of 2007, our instincts had been telling us it was 'only a matter of time' before the bull market ended. Although we felt strongly that the end of the boom was imminent and that the consequences would be worse than those following the 1987 crash, we did not have a sense of when this would occur or what the trigger would be. I regret that we did not back our judgement more and take steps to profit from the collapse but I take comfort in knowing that we have avoided much of the harm that might have come our way had we responded to market pressure to grow funds under management and go after scale without regard to risk."

- Seph Glew (Chairman)

"A constant theme within our business since I joined in early 2000 has been the late 1980's correction and its consequences to the Australian property and financial markets. For this reason, I believe that I and our younger senior executives have had a unique insight into the lead up to the current market

¹ In 1993 Seph Glew co-founded Jagar Property Group with Paul Tressider, in addition to Wynn Tressider Management alongside Guy Wynn and Paul Tressider.

² Harrington Partners Fund 1 also owns shares in BWR

³ BlackWall Limited [ASX: BWF] 2019 Annual Report - <http://www.aspecthuntley.com.au/asxdata/20190826/pdf/02138296.pdf#search=%22%22>

conditions. As a consequence, our team is viewing this turmoil as more of an opportunity than a threat.”

- Stuart Brown (CEO)

This investment committee delivers enormous value for all BlackWall shareholders, and our impression is that they have the energy and desire to keep diligently applying their wisdom for many years to come. This is especially true under the current circumstances where they have direct access to upwards of \$100 million of investable capital within BWR that enables their aggregate judgment to be leveraged at several multiples of what has been achievable in the past. Importantly, the patient owner-operator mentality of this founding group has been passed on to the broader executive team in Tim Brown, Jess Glew, and Sophie Gowland, all of whom appear highly capable of leading BlackWall through the next era of growth.

We believe that building a coordinated management team of BWF’s calibre with comparable capital allocation and operating skills, alignment of incentives, energy, and inherent credibility would take at least a decade or more. And if you succeeded in developing such a team, you would inevitably still be well behind what BWF will likely become through another decade of compounding these powerful fundamentals. Fortunately, we do not have to take such risks as we have the opportunity today to partner with an established team that meets this ideal, at what seems to us to be a reasonable price.

While a first-class management team is crucial, the long-term economic outcomes they achieve will inevitably be tethered to the business model they adopt, the underlying performance of the industry in which they operate, and their competitive strength as part of this overall dynamic. On this front we must be clear in stating that we believe there is a high probability the Australian commercial property market will see a meaningful correction in the near future. Fortunately, under this scenario it seems likely that BWF will thrive as the demand for their somewhat unorthodox skillset should rise substantially.

“With property yields at record lows we think it unlikely that BWR will acquire passive real estate investments in the near term, but we are on the hunt for active investments and special situations where we believe we can succeed regardless of market conditions... In our view, commercial property yields are at unsustainably low levels and a correction is coming. Our aim is to be ready to act when investors are most fearful.”⁴

In our view BWF has very attractive investment potential as it is ideally positioned with the business model, management, and financial capacity necessary to exploit an inevitable torrent of great opportunities that will emerge from the next round of property market turbulence. We are hopeful that both Blackwall Limited and BlackWall Property Trust will become core portfolio holdings for Harrington Partners and prove to be a brilliant long-term investment that deliver both above-average income and capital growth.

Gowings Brothers Limited [ASX: GOW] is a Sydney based listed investment company which began its life as a department store operator in 1868. The Gowing family has guided the Company for its entire 150-year history with the current managing director and largest

⁴ BlackWall Property Trust [ASX: BWR] 2019 Annual Report - <http://www.aspecthuntley.com.au/asxdata/20190826/pdf/02138301.pdf>

shareholder John Gowing being at the helm for the last 32 years. The company has several of the key fundamental characteristics we seek namely; robust balance sheet, large insider ownership, competent capital allocation, and growth potential - all at a reasonable price.

GOWs investment portfolio is concentrated within two wholly owned sub-regional shopping malls situated within the central business districts (CBD) of Coffs Harbour and Port Macquarie which respectively are the 24th and 30th largest population centres in Australia.⁵ These assets are certainly not 'prime' real estate given the combination of concentrated exposure to retail tenants, regional locations, and inherent interest rate sensitivity. They are, however, sensibly financed and have good long-term potential given they occupy large and prominent CBD locations within these increasingly popular coastal locations.

The redevelopment options afforded through free-hold ownership enables GOW to proactively repurpose these assets over time. In some cases, this is already occurring with the recent redevelopment of Coffs Central incorporating two levels of office space that currently houses the headquarters of one of the region's largest credit unions. We expect this pragmatic approach to growing shareholder value will continue due to the dual incentive of concentrated insider equity ownership and the desire to uphold a proud family legacy.

"Gowings is an investment company whose investment horizon is inter-generational. In fact, Gowings has had only four managing directors since its establishment in 1868. Being a shareholder in Gowings is for investors who share a similar investment philosophy and who wish to invest alongside the Gowings family. An important investment philosophy is to generate sustainable and reliable dividends that can provide income for shareholders." – FY19 Annual Report

The company also has a diverse portfolio of property development, public and private equity, and venture capital investments which together look set to provide ongoing benefit for shareholders. The most significant of the property development assets is a 220-lot residential subdivision known as [Sawtell Commons](#) where the 7 lot display village is under construction and the first release of 60 lots is now selling. Further, GOW are currently investigating the development potential of vacant land adjoining Port Central and also own a large development site in the 'Jetty Precinct' of Coffs Harbour currently under planning application. Each of these opportunities has the ability to generate compelling value for shareholders although they will require substantial amounts of capital, patience, and managerial commitment to see through to successful completion.

GOWs largest private equity investments include their wholly owned operating subsidiary known as [Surf Hardware International](#), and a large position in Australia's preeminent olive-oil company known as Boundary Bend (owner of the Cobram Estate and Red Island brands). Outside of these primary exposures, GOW has a diverse range of direct property and equity investments that collectively have a book value that equates to around 30% of the current market capitalisation.⁶

⁵ https://en.wikipedia.org/wiki/List_of_cities_in_Australia_by_population

⁶ This assumes FY19 book value for Kempsey Central, 'Other' property, and remaining private & public equity holdings.

We expect GOW will be a steady long-term performer that distributes regular fully franked income and is likely to appreciate in fits and spurts if and when their myriad of capital growth opportunities come to fruition. These somewhat 'average' characteristics means GOW is unlikely to ever become a large holding in the Fund, however at present they are attractive due to the combination of their fully franked yield, the development potential and what appears to be a meaningful net asset discount.

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