CI GLOBAL EQUITIES FUND (UNHEDGED)
QUARTERLY REPORT

Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

JUNE 2014

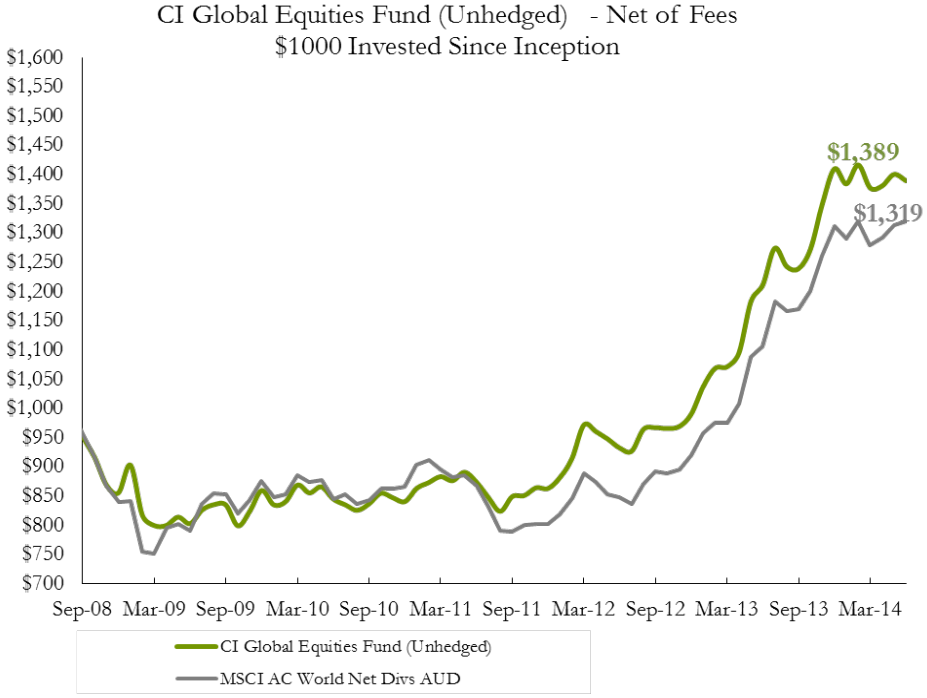
"It is not from the benevolence of the butcher, the brewer or the baker that we expect our dinner, but from their regard to their own interest." Adam Smith

"The risk among any group of investors is that they only pay attention to what they already agree with." Michael Mauboussin

"It's not during up years that great investment track records are made." Charles de Vaulx

	****PORTFOLIO**	**#BENCHMARK**	**VALUE ADDED**
ROLLING 3 MONTHS	1.33%	3.15%	-1.82%
ROLLING 1 YEAR	16.21%	19.24%	-3.03%
ROLLING 2 YEAR	23.58%	24.78%	-1.20%
ROLLING 3 YEAR	18.07%	14.98%	3.09%
ROLLING 5 YEAR	12.80%	10.80%	2.00%
SINCE INCEPTION*	6.84%	4.86%	1.98%
SINCE INCEPTION^	47.07%	31.90%	15.17%

*Annualised
^Cumulative (1 September 2008)
**Before fees and expenses
MSCI AC World Net Divs AUD



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Market and Portfolio Performance

At the headline index level it was a relatively benign quarter with global equity markets gaining around 4% and volatility (as measured by the 'VIX' Index) declining to a seven year low.

Indeed this year has been characterised by asset prices generally ticking up within tight ranges accompanied by unusually low levels of volume. We have observed some rotation this quarter – for example large caps outperformed small caps in both the U.S and Europe, reversing the trend of the last twelve months and suggesting more caution amongst investors.

However the real action has been taking place across the 'Chinese walls' from the trading floors; on the desks of investment bankers.

We have seen an explosion in corporate activity year to date - per numbers from *Bloomberg,* there have been over 10,000 global M&A deals done in 2014 for a total value of $2trn. This is up nearly 90% from the prior year. Further, considering only deals of value greater than $1bn, there have been 467 deals, up 60% year on year. By region, the U.S. has seen $827bn of deals (+85% YoY) while Europe has seen $765bn of deals (+132% YoY). This year has comfortably been the highest M&A spree since 2007.

One clear emerging trend is that of the 'tax inversion'; of the top five deals announced by value in 2014, four have been in the healthcare space (AstraZeneca/Pfizer, Allergan/Valeant, Abbvie/Shire, Covidien/Medtronic). Of these, three involve a U.S.-based company taking over one located within the British Isles, ostensibly for the purposes of moving to a lower tax domicile. We saw this happen two years ago with **Aon**, and while for Aon it makes good sense for the majority of its people to be near the London insurance market, we wonder about the long term operational wisdom of moving a global pharmaceutical headquarters to the cobbled streets of Dublin.

A number of deals have involved our portfolio companies. In Europe, **Nestlé** has been busy building up its skincare and nutrition portfolio (a stated area of focus for management) with the consolidation of the existing Galderma JV from L'Oreal followed by the $1.4bn purchase of Sculptra, a portfolio of anti-wrinkle products from Valeant. We have also seen ongoing bolt-on acquisitions from **Assa Abloy** buying an Indian lock brand and **Diageo** completing the acquisition of United Spirits.

Over in the U.S. **Oracle** has just paid $5.3bn for retail tech company Micros Systems, while both **Time Warner Inc.** and **International Paper** have been spinning off non-core parts of their businesses. Not to mention the ongoing merger in which **Comcast** will acquire Time Warner Cable, as discussed in last quarter's newsletter.

While we encourage value accretive M&A, we also watch companies carefully for financial discipline; often more insight into management's judgement can be gleaned from the deals they *don't* do than the ones they do. In April, **Reckitt Benckiser** became embroiled in a bidding war with German peer Bayer for Merck's branded consumer healthcare assets. As the valuation spiralled beyond €14bn or 25x EV/EBITDA, Reckitt pulled out of negotiations; a great example of 'keeping one's powder dry' by CEO Rakesh Kapoor.

Nevertheless, with significant cash piles on hand and in a world of low growth and zero interest rates, we are not entirely surprised to see boards signing off on all these deals.

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The Portfolio

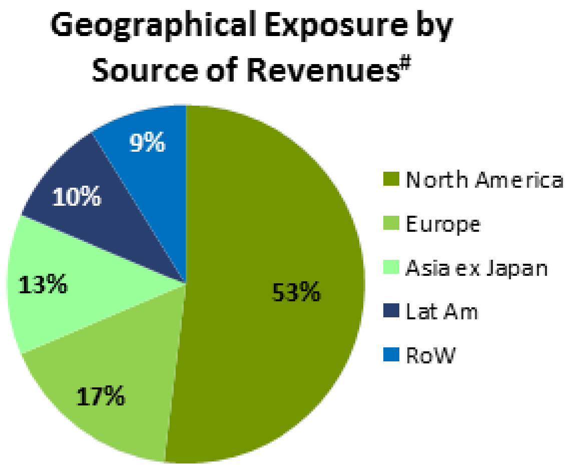
The portfolio returned 1.33% during the quarter vs the benchmark which returned 3.15%.

The AUD continues to appreciate in 2014, rising 2% against the USD and 3% against the EUR, whilst remaining flat vs the GBP and JPY during the quarter. The AUD is up 5.5% vs the USD year to date.

The three biggest outperformers this quarter in terms of total shareholder return were **Unibail-Rodamco, Remgro** and **Prosegur Seguridad**. The main underperformers by total shareholder return were **Domino Printing**, **Close Brothers** and **eBay Inc**.

The portfolio is diversified by both country and sector. In order to more appropriately represent from which countries the portfolio generates earnings, we derive the following pie chart from Company accounts and disclosures.

No. of Stocks	**42**
Region Weights	**U.S. 54%**
	Europe 28%
	Asia ex-Japan 3%
Most OW Sectors	**Financials, Industrials**
Most UW Sectors	**Energy, Health Care**
Cash	**4%**



#Derived on a look-through basis using underlying revenue exposure of individual fund stocks

Portfolio Changes

We added 2 new positions this quarter; **W. W. Grainger** (MCap $17bn) and **British Sky Broadcasting** (MCap $24bn).

Grainger is a leading distributor of maintenance, operations and repair products ("MRO"). We have been following Grainger since management first walked through our Collins St. office three years ago, and every year since have been back to visit their Chicago headquarters. This year was no different as we walked out of the meeting with a positive view of Grainger and its future. However, today we can see a clear value proposition. The shares have stagnated over the past 12 months while the business continues to progress. In the meantime the market has powered ahead a further 20%. After years of building up our knowledge base we decided now was the right time to buy.

Grainger is a business to business distributor of products used to maintain, repair or operate many kinds of facilities. They are the market leader in the U.S. where they first began distributing industrial supplies (safety gloves, cutting tools, etc.) way back in 1927. Since then the business has established unmatched size and scale with a clear market leading position – Grainger catalogues and distributes 1.2m different products and serves a wide customer base including healthcare, manufacturing, government and hospitality. The industry is so large that despite its number one status Grainger makes up only $7bn of revenues in a $140bn market. There is a massive growth opportunity in a business that generates 50% returns on invested capital.

Given the growth opportunity of the U.S. operations we believe shareholders are paying nothing for Grainger's international businesses, which are almost a quarter of group sales. These are a mix of established operations (Latin America & Canada), barely profitable businesses (China & Europe) and a controlling stake in Japanese-listed MonotaRO, who we also visited in Osaka this quarter and which is worth almost $1bn. We believe that as shrewd allocators of capital, Grainger will look to sell or restructure any underperforming business. We think these initiatives will turn a more positive view on the non-U.S. portion and Grainger as a whole, giving the share price its just deserts.

Early in the quarter we initiated a position in **British Sky Broadcasting plc** ("Sky"). Sky is the leading Pay TV distributor in the U.K. with around 70% market share of the Pay TV market, equating to 11.2mn subscribers. Sky's delivery mechanism is via Direct-to-the-home satellite, the most efficient, capital light and highest quality distribution method for Pay TV. Sky also has 4.9mn fixed line broadband subscribers - the so-called 'triple play' - which it is capturing via BT's unbundled local copper network.

The business model is appealing – 90% of revenue comes from post or pre-paid residential or wholesale consumers, with a churn rate of 10-11%, one of the lowest in the industry globally.

We have built up an extensive internal knowledge base over the years around Pay TV ecosystems, both on the distribution and content side – the portfolio has owned both Time Warner Cable and Comcast in the U.S, while our colleagues in the Australian Equities Portfolio have invested in 21st Century Fox ("FOX") and Sky New Zealand over a number of periods.

We note that the U.K. market structure is potentially one of the most attractive we have seen. It has one premium player controlling the lion's share of the market, whereas in the U.S. competition is much more intense with sometimes four or five players competing for wallet share. In terms of penetration, the U.K. at around 55% looks low compared to the U.S. at 90%.

Sky have been growing their subscriber base by offering innovative new products (such as Sky Go on the iPad) while maintaining product leadership with the best quality HD set-top-box, significantly better customer service than peers, and the widest range of content through exclusive deals with the main U.S. movie and TV-show studios.

As an asset-light business, Sky delivers returns on equity close to 100% and has an under-geared balance sheet. Revenue is growing 5-6% per annum and the business is extremely cash generative – over the last five years it has generated on average £830mn of free cash flow per annum which is roughly equal to net income. The company yields a 7% cash return per annum to shareholders via dividends and buybacks.

Despite the stability of earnings, Sky's stock price has been relatively volatile recently which provides long term-oriented investors with opportunities. Indeed, Sky has been hit by two major issues in the last 3 years both of which de-rated the stock.

First, Rupert Murdoch (Chairman and CEO of FOX, a 39% stakeholder in Sky) is a high profile figure in the U.K. and the British media loves to bash him. The 2011 News of the World hacking scandal led to a media circus culminating in a risk to Sky's broadcasting license. This risk was ultimately unrealised, though it did lead to a more formal separation of the Murdoch's broadcasting and newspaper empire.

Secondly and more recently, Sky has been taking market share from BT Group's fixed wireline business by allowing customers to bundle Sky Broadband with their TV package at attractive prices. As a strategy to counter this, BT Group launched a Pay TV business ('BT Vision') and in late 2013 bid aggressively for both English Premier League ("EPL") and Champions League football rights which it now effectively gives away for free to broadband customers as a retention tool.

This led to a further de-rating of Sky as analysts extrapolated BT's behaviour into becoming a major competitor to Sky in the Pay TV sphere.

Worries over an ensuing sports rights war have supressed the Sky share price for a year and are providing the opportunity for accumulation of a cash annuity business at a discount to intrinsic value or around 8x forward EV/EBITDA.

Our view is that a major skirmish will not erupt between the two players, and that BT is satisfied that its initial foray into sports rights has stemmed the bulk of the bleeding of broadband losses and therefore has achieved its objective. Rather than having major ambitions to supplant Sky as the premium U.K. Pay TV provider, our read is that with 2 out of 7 EPL packages, given the cost of these rights, BT's significant pension deficit, and the lack of proof that it can yet monetise its expensively assembled content, BT will be happy to maintain the status quo in the next EPL auction.

While the recently mooted 'Sky Europe' merger with Sky Deutschland and Sky Italia is a consideration, this has been long in the company's mind and is not really a new development. We will reserve judgement until concrete numbers are announced but note that, love him or hate him, Murdoch has made himself and his shareholders rich from a career of doing deals like this.

The portfolio exited entirely from two stocks in the quarter; **Mattel** and **Vodafone**.

The original thesis for buying **Vodafone** back in mid-2012 was the inherent value of the Verizon Wireless JV that was hidden within the sprawl of the group. The cash flows from this asset were substantial and we felt the market did not appreciate the value of these, either in a yield sense or in the potential for Verizon to buy Vodafone out of the JV. That did indeed transpire earlier this year in the largest M&A deal of the decade, and after receiving a chunk of cash and Verizon shares the portfolio's position in Vodafone was naturally reduced.

Looking at 'residual Vodafone' we see a number of impending structural and management challenges in the European businesses. While we acknowledge the group's emerging market businesses are doing well, we conclude that we don't want to own the sum-of-the-parts here and see better opportunities elsewhere.

Mattel was sold post a disappointing 2013 result. Since investing in Mattel in 2011 the company had made positive strides by lifting its margin, making some smart M&A moves, further penetrating into emerging markets and returning all free cash flow to shareholders. However, in Q4 Mattel failed to execute for a number of reasons in the all-important holiday season. Given the nature of its business, an inventory build-up of unpopular stock has been created which we think will take a number of years to work through.

Stock News

As mentioned previously both **Time Warner Inc.** and **International Paper** spun off non-core divisions into separate listed companies. The portfolio subsequently sold both of these new listings (International Paper distributed its spin-off company on July 2 and was sold on July 7).

In what looks to be the final piece of the Time Warner AOL break up, Time Inc. was spun off from Time Warner and listed. Time Inc. is the publishing assets (predominantly magazines) leaving Time Warner as a pure play TV and film business. This new pure play has greater exposure to more predictable and faster growing subscription revenue streams as well as a higher margin business, which should command a higher multiple. We favour companies that slim down and focus on their core.

As for Time Inc., the new company will likely get a new zest for life as it lacked the necessary investment as part of a larger entertainment conglomerate. However, the balance sheet carries uncomfortable levels of gearing for a business that continues to decline and is subject to advertising cycles, and thus the portfolio sold its shares immediately on receipt.

International Paper separated its distribution business into a new listed entity. This was a more complex transaction as it merged with another company at the same time creating the newly formed Veritiv Corp. Given the small size of Veritiv (Mcap of $300m) we had no interest in retaining the shares.

We note that historically, this low margin distribution business has partially concealed the strong performance of International Paper's core box packaging business. The removal of the distribution assets will see group EBITDA margins immediately increase from 14% to 18%. We think this will help the market recognise the value and profitability of the box business. International Paper's current multiples (12x free cash flow, 6x EBITDA and 1x EV/sales) suggest this is not being fully appreciated.

During the quarter **GEA** reported the sale of its Heat Exchangers segment to Triton, a U.S.-based private equity fund for €1.3bn. Heat Exchangers were one of GEA's lowest return on capital businesses, and the power industry on which this division depends is going through a major slump.

By selling this non-core asset, GEA becomes more than 70% exposed to food and beverages, an area with better prospects and that more appropriately reflects GEA's evolving strategy. This disposal was part of the original thesis and we are pleased to see management execute in a timely manner and realise good value for shareholders from an underperforming asset. The sales proceeds will lift GEA into a net cash balance sheet position with firepower for either bolt-on M&A or cash distribution. The market took the news favourably with the stock up 10% in the last four weeks, while management will address the market with their strategy in mid-July.

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Trip News

During this quarter we travelled to both the U.S. and Japan.

In the **U.S.** we spent two weeks in the Midwest. Seeing the industrial heartland of Illinois and Minnesota provided an additional perspective to the financial and tech centres of the East and West coasts. We came away with a positive tone from the industrial companies we visited.

It is clear that, not only does the U.S. still have a role to play as a globally relevant manufacturing hub, but is in fact strengthening this position after a decade of offshoring (see chart below). This has follow on implications as it affects adjacent industries such as packaging (International Paper) and transportation (UPS).

Source: US Bureau of Labor Statistics

On the other side of the equation low rates continue to be pushed out further which is impacting a number of businesses. Industries that rely on interest and float income continue to see revenue streams under pressure. In the financial world it is not only the major banks that are seeing net interest margin pressure but custody and trust banks too. More so these businesses have to waive fees on a range of products as fees are greater than interest rates.

The standout meeting was an afternoon spent at a company called Videojet, a subsidiary of Danaher Corp. Danaher has been a long time investment and a large position in the portfolio. Danaher is unique in that it does not define itself by an industry or product but rather a process; the Danaher Business System "DBS". Danaher makes and sells all sorts of instruments; blood testing machines, dental equipment, water treatment kits, petrol pumps and many, many other devices. Videojet manufactures product identification equipment that makes barcodes and use-by-date labels. DBS is a set of tools made up of Danaher's best practices that can be applied to just about any instrumentation business: "It is common sense rigorously applied".

Danaher's business model is to deploy the majority of its free cash flow into acquisitions using the DBS process to generate improvement and returns at the acquired company. With a balance sheet almost in net cash position Danaher has stated it has over $8bn of M&A firepower. If the company deploys this capital at an acceptable return Danaher is trading closer to 13x free cash flow as opposed to the 16x headline number we see today.

Given that Danaher's ability to deploy cash into M&A is key to the value proposition, visiting the Videojet facilities was an extremely useful exercise. Danaher has built itself into a powerhouse that generates $20bn of revenues today by doing this exact thing repeatedly over the last 30 years. Videojet itself was a major acquisition back in 2002. Being walked through Videojet's progress over the last 12 years helps provide an understanding and confidence of how and why Danaher can replicate this success.

It is several years since we visited **Japan**, and with the country in the midst of a massive reflationary attempt by the government, it was a particularly timely trip.

Much has been written about 'Abenomics' since President Shinzo Abe came to power in late 2012, so in the interests of brevity we will not cover the topic here or make predictions about whether Abe's policies will work or not. Frankly, nobody knows. What is clear though, is with sovereign debt in excess of 230%-to-GDP and a generation of people who hoard cash in the anticipation of falling prices, Japan is fiscally in the 'Last Chance Saloon'. Our trip was focused on visiting corporates and getting a sense on the ground of whether economic reform is starting to be genuinely felt.

One major criticism levelled by global fund managers at Japanese companies regards capital allocation. The view is that Japanese boards don't care about shareholders and tend to destroy capital; that the share price and total shareholder returns are less important to Japanese board members than maintaining the status quo and serving on the board until a ripe old age. Indeed, there is much evidence for this, though from our trip we would counter that change is, finally happening.

We are pleased to see a number of reforms occurring, for example around governance, shareholder stewardship and the role of equity in the capital structure. For example, a new stewardship code has been released by the aptly titled *"Council of Experts Concerning the Japanese Version of the Stewardship Code*" which includes guidance for fund managers around their fiduciary responsibilities to clients. We note that the largest government pension scheme, the GPIF, has not only been increasing its weighting in equities recently, but is appointing active managers who are benchmarked on the new ROE-focused JPX Nikkei 400 index.

We also note an increased focus on cash returns to shareholders – since 2012 over $50bn worth of buybacks have been announced by Japanese companies, many of which are buying back and cancelling 5% or more of their outstanding shares. In addition, Japanese companies are paying more dividends than ever before, and several we visited are explicitly targeting a yield of 3% or more. In fact in almost every company meeting we attended, the topic of cash returns to shareholders was acknowledged as important by the company and an area of ongoing focus for the board.

Another commonplace view on Japan is that there is no domestic growth. However we found many pockets of growth which represent potentially interesting areas of investment opportunity. Many of these are linked to the changing demographics of the country, and while the fact that the Japanese are aging faster than any nation on Earth is no secret, participating in a tour of a large suburban pharmacy and seeing the rows upon rows of walking sticks and Zimmer frames really brought this home. In fact, not only are people living longer, they are increasingly living alone. Thus:

- From 2000 to 2012 the over 60's population grew 38% vs flat total population growth (Sugi Holdings)
- From 1995-2010 single occupancy households grew 27% (Daiwa House)
- Like-for-like growth of prescription dispensing in pharmacies is growing 15% p.a.
- Convenience store space is growing 5% p.a. (Lawson)

We think both the convenience store and pharmacy store businesses are attractive areas to invest and are looking closely at a number of ideas in these and other sectors.

We continue to be invested in Japanese power tool maker Makita, which is benefitting from a number of tailwinds including:

- Infrastructure build-out in emerging markets, many of which Makita dominate, has gathered pace after a post-GFC lull
- The recovery in housing and construction in both the U.S. and Europe
- Ongoing Tōhoku Earthquake reconstruction efforts in North East Japan
- The weak Japanese Yen (83% of sales and 66% of profits are outside of Japan).

The stock is up 142% in local currency since the position was bought but will be maintained in the portfolio for now as we continue to see growth opportunities both at the top line and for profit margins.

We were impressed by the humility and cost focus on display at Makita's headquarters in Anjo, Aichi Prefecture, and were particularly struck by the wisdom and simplicity in co-founder Jujiro Goto's personal credo, which we think is worth sharing:

- Don't be angry – 'Okoruna'
- Don't be arrogant – 'Ibaruna'
- Don't panic – 'Aseruna'
- Don't mope – 'Kusaruna'
- Don't give up – 'Makeruna'