

ANNUAL REPORT
December 31st, 2018
(Potential Clients)

This report is intended for people interested in making an initial investment in either the **HughesLittle Value Fund** or the **HughesLittle Balanced Fund**. This report does NOT provide an overall explanation of the Funds nor a detailed description of our investment approach. That information can be found in other documents on our website.

This report is produced quarterly. It contains up-to-date information we think you should understand when assessing making an investment with us. Reports from previous quarters can be found on our web site.

If you do not wish to receive these reports or have any questions, call us at 1 877 696 9799.

2018 Performance

To December 31st, 2018 the change in unit prices of the **HughesLittle Value Fund** and **HughesLittle Balanced Fund** were as follows:

| | Value Fund <i>(non-RSP)</i> | Balanced Fund <i>(RSP)</i> |
|--|---------------------------------------|--------------------------------------|
| Post-Distribution Unit Price | \$35.13 | \$18.91 |
| 2018 Distribution | \$ 0.02 | \$ 1.07 |
| Pre-Distribution Unit Price | \$35.15 | \$19.98 |
| Unit Price on December 31 st , 2017 | \$32.17 | \$18.67 |
| Total Distributions Since Inception | \$ 2.48 | \$ 8.67 |
| One Year Return | 9.3 % | 7.0 % |
| Annualized Return Since Inception¹ | 11.1 % | 10.3 % |

See attached Performance Summary for additional performance results.

¹ Inception dates: Value Fund June 30th, 2005. Balanced Fund August 31st, 2005.

Commentary

The underlying financial results of the Funds' portfolio companies in 2018 ranged from decent-to-exceptional. In many cases, underlying corporate performance exceeded share price performance.

In our view, assessing the underlying performance of a Funds' portfolio companies is the proper way to assess the progress of our Funds, or any Fund. A Fund is just a conduit to what you are really investing in - a portfolio of operating businesses. And if those businesses are held long enough by the Fund, and generate decent growth in revenue and profits, you will also achieve decent growth in your investment.

This is a distinctly different and far more useful way to assess a Fund than simply looking at a change in unit price - especially over a short period of time. Short-term changes in our Funds' unit prices are driven by short-term changes in share prices. And in our experience, short-term changes in share prices are random at-best, rarely reflect actual changes in the fundamentals of the companies themselves, and for sure tell you nothing about a Fund's return prospects.

One development in 2018 that has and will continue to have a positive impact on many of our companies' fundamentals was the lowering of the corporate tax rate on income earned by businesses in the United States. Briefly, starting January 1st, 2018 U.S tax law eliminated the previous tiered tax structure that had an upper limit of 35 percent on U.S. corporate income. It was replaced with a flat corporate tax rate of 21 percent along with fewer exemptions and deductions.

The vast majority of our portfolio companies earn income in the U.S. Those companies now pay substantially lower taxes on their U.S. income. This was, by far, the biggest driver of profit growth last year.

As an example, two of the Funds larger holdings operate solely in the U.S. (they have no foreign income). One is a financial services company and the other is in consumer products. For these two, their tax savings are substantial as nearly all their operating profits are now taxed at the new rate (about one-third lower than the old rate). This is where it gets interesting. *Based on results so far, we estimate the tax savings alone have boosted the intrinsic value of both companies by about 25 percent.*

Price Versus Value

An important theme in these reports and to our investment approach, is thinking rationally about price and value. When we refer to “price” we mean the market price of a company’s common shares as quoted on a stock exchange. “Value” on the other hand, has no quoted number, it is an estimate of a company’s underlying or intrinsic value. This estimate is based on the expected profits a company will generate for its owners over the life of the business.

We use the concept of “intrinsic value” in two ways. Firstly, in our experience, long-term gains in a company’s intrinsic value is the primary driver of gains in a company’s share price. So “potential growth in intrinsic value over the long-term” is a key consideration when selecting companies for the Funds.

The concept of intrinsic value also plays a part in our buy and sell decisions. In practice, once we’ve estimated a company’s intrinsic value, we’ll compare the intrinsic value to the company’s share price. Share prices that discount intrinsic values may be candidates for purchase. Share prices that exceed intrinsic values may be candidates for sale.

Throughout 2018 the Funds’ portfolio companies generated financial results that would indicate another year of steady gains in intrinsic values, as well as, evidence these gains will continue. Share prices on the other hand, were much more volatile. Over the course of last-year, we saw many share prices dip to levels that presented us with attractive price-to-value discounts. As a result, the Funds added to several existing holdings and invested in two new companies. By year-end both Funds were fully invested in common stocks, reflecting what we believe to be favourable risk/return prospects.

Portfolio Review

As of December 31st, the Value Fund was 100 percent invested in 15 operating companies. The Fund owns four Canadian companies, eight U.S. companies, and three holdings based in other countries. The Value Fund’s top ten positions make-up 88 percent of the Fund’s assets.

The Balanced Fund is 81 percent invested in the common shares of four Canadian companies, seven U.S. companies, and four companies based in other countries. The Balanced Fund’s top ten positions make up 70 percent of the Fund’s assets. At year-end the Balanced Fund had 19 percent of its assets in cash and investment grade bonds.

2018 Distribution and an Update on Capital Gains

Distributions for 2018 are \$0.02 per unit for the Value Fund and \$1.07 per unit for the Balanced Fund. The Value Fund's distribution is entirely Canadian dividend income, zero capital gains.

The Value Fund has experienced nine out of fourteen years of operation where it has not distributed any realized capital gains to unitholders. One consequence of not regularly *realizing capital gains* within the Value Fund is a build-up of *unrealized capital gains*. As of December 31st, 2018, the per-unit value of unrealized capital gains in the Value Fund is \$16.13.

It is impossible for us estimate or speculate on how long we will carry-forward these unrealized capital gains. One of our companies for instance, could be taken over and we are forced to sell our shares. That would trigger a *realized capital gain* that would likely benefit the Value Fund's longer-standing unitholders more than the Fund's newer unitholders.

What we will continue to do however, is run the Value Fund as we always have: with an objective of earning a satisfactory long-term, after-tax return for the Fund's unitholders. Taxes can be a very substantial cost to investors in any Fund, and we seek to manage those costs for the benefit of all our unitholders (us among them).

Fund Expenses

The 2012 to 2018 Management Expense Ratio (MER) for each Fund was as follows:

| | 2018 | 2017 | 2016 | 2015 | 2014 | 2013 | 2012 |
|----------------------------|-------|-------|-------|-------|-------|-------|-------|
| HughesLittle Value Fund | 1.15% | 1.15% | 1.16% | 1.17% | 1.18% | 1.23% | 1.28% |
| HughesLittle Balanced Fund | 1.21% | 1.23% | 1.23% | 1.24% | 1.25% | 1.33% | 1.38% |

The MER reflects all expenses charged to the Funds throughout the year. These expenses include: investment management fees, audit, trustee, custodian, administration, and GST/HST. Details of these expenses are disclosed in the Funds' year-end financial statements.

The MER is expressed as a percentage of the average assets within each Fund over the entire year. The performance results we report are after deducting these Fund expenses.

Miscellaneous

If you are planning on making an investment in either HughesLittle Fund, please call us and we will assist you with all the required application and/or transfer documents. Our toll-free number is:

1 877 696 9799

If you have any questions or comments, we welcome your calls or visits.

Regards,

Joe Little
January 8th, 2019

Mark Hughes