Flinders Emerging Companies Fund

Monthly Update: August 2017

FLINDERS
Investment Partners

Performance *(after all fees and expenses)*	**1 Month** (%)	**3 Months** (%)	**1 Year** (%)	**Since Inception^** (% pa)
Flinders Emerging Companies Fund	4.8%	5.9%	-6.2%	10.4%
S&P/ASX Small Ords Accumulation Index	2.7%	5.1%	3.2%	15.2%
Net Value Added	**2.1%**	**0.8%**	**-9.4%**	**-4.8%**

^ Inception date is 30 September 2015. Past performance is no indicator of future performance. Information relates to the Flinders Emerging Companies Trust Class B.

Investment Objective

Exceed S&P/ASX Small Ordinaries Accumulation Index by 5% pa (pre-fees) over rolling 3 year periods

Investment Time Frame

5 years

Portfolio Managers

Andrew Mouchacca and Richard Macdougall

Risk Profile

High

Distribution Frequency

Half Yearly

Minimum Investment

$25,000

Inception Date

30 September 2015

APIR Code

ETL0449AU

M-Funds Availability

Code FEC01

Responsible Entity

Equity Trustees Ltd

Research Ratings

Lonsec: Recommended
IRR: Recommended
Zenith: Approved

Platform Availability

CFS, MLC, Netwealth, Powerwrap, HUB24, Macquarie Wrap

Further Information

www.flindersinvest.com.au
or +61 3 9909 2690

Flinders Investment Partners Pty Ltd
Level 15, 385 Bourke Street,
Melbourne, Vic 3000
www.flindersinvest.com.au

- **Small caps gaining strong momentum over large caps**
- **Resources strong – gold up on North Korean tensions**
- **Reporting season – FY18 growth upgrades**

Market

Small caps (+2.7%) outperformed large caps (+0.5%) meaningfully in August, extending the trend to four months. Within small caps, resource companies (+7.1%) strongly exceeded industrials (+1.7%). Continued advances in commodity prices underpinned the move, with gold up on North Korean tensions, and base metals / iron ore up with better than expected growth data from China. The small resources sector is in its best shape in years. Balance sheets of resource companies are flush with cash (65% are net cash compared to only 24% for industrial companies) and hence these companies are better capitalised to withstand any volatility in commodity markets. In addition, the recent rally in commodity prices has not translated fully to consensus estimates which remain low and as such valuations remain appealing.

Reporting season was lacklustre; expected earnings growth for small caps in FY17 was 16.0% growth going into reporting season, and was subsequently revised down to 10.5% post reporting season. For companies that observed downgrades, common reasons cited included foreign exchange headwinds and softer consumer demand. Importantly, expected earnings growth in FY18 was upgraded over the result period from 9.0% to 12.5%. The upgrades came from both industrials (11.5% from 9.2%) and resources (19.0% from 8.0%). To put this in perspective, large company earnings are expected to grow only 3.7% in 2018 – that should put pressure on the sustainability of dividend payments for that segment and ensure that the recent trend of outperformance of smalls over large caps continues. Indeed, large 'bluechip' companies such as Telstra, Commonwealth Bank and Woolworths were the big disappointers during reporting season.

Portfolio

The Fund performed strongly over the reporting season, returning +4.8% for the month and outperforming the benchmark by +2.1%. Drivers of Fund outperformance included:

1. exposure to resources companies and associated service providers;
2. avoiding companies that disappointed the market in their earnings delivery and/or their outlook statements; and
3. holding companies that delivered a beat to market expectations or conveyed a positive growth outlook.

Key Contributors: Software company **Altium** (+13.9%) delivered a result that exceeded expectations. We have held the company since we launched the Fund, and it continues to be a consistent performer with strong earnings growth and operational leverage evident. Salary packaging company **Smartgroup** (+18.8%) has developed a reputation of under-promising and over-delivering, and this result demonstrated good organic coupled with growth from successful acquisitions. **New Century Resources** (+87.4%) has one of the largest zinc deposits in the world and its backdoor listing onto the ASX during the month has gone largely unnoticed. The company is well funded and has minimal capex requirements to recommence production in mid-2018. Iron ore contractor and lithium miner **Mineral Resources** (+23.6%) delivered a strong result with guidance for FY18 above consensus.

Key Detractors: Media monitoring company **iSentia Group** (-20.7%) was one of the main disappointments for the Fund. The stock was purchased at depressed levels in May when the company reiterated guidance, yet the result fell short of expectations. We exited the holding (at a price higher than our entry price). Comparison service provider **iSelect** (-17.2%) fell slightly short of expectations (still within the company's guidance range), citing a weaker consumer earlier in the year. We continue to like the business they are building, as well as the associated strong growth profile, and so retain a holding. **The A2 Milk Company** (+21.7%) and **Whitehaven Coal** (+17.8%) were not held in the portfolio, yet were detractors given their strong price appreciation and meaningful weights in the benchmark index.

Performance Attribution^		Top 5 Active Positions^
Top 5 Contributors	Top 5 Detractors	
Altium	A2 Milk Company*	Altium
EML Payments	Catapult Group International	Mineral Resources
Mineral Resources	iSelect	Service Stream
New Century Resources	iSentia Group	Speedcast International
Smartgroup Corporation	Whitehaven Coal*	Webjet

^ Alphabetical order * Denotes stock not held

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