Flinders Emerging Companies Fund

Quarterly Update: September 2016

FLINDERS
Investment Partners

Performance *(after all fees and expenses)*	1 Month (%)	3 Months (%)	6 Months (%)	Since Inception^ (% pa)
Flinders Emerging Companies Fund	3.9	11.1	23.3	33.8
S&P/ASX Small Ords Accumulation Index	1.5	8.5	14.8	29.2
Net Value Added	**2.4**	**2.6**	**8.4**	**4.7**

^ 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: Investment Grade
Zenith: Approved
IRR: Recommended

Platform Availability

Powerwrap, HUB24, Macquarie Wrap

Further Information

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

- **Spring rally**
- **Reporting season optimism**
- **RBA cuts rates in August, Fed to raise rates?**

The Flinders Emerging Companies Fund ('Fund') performed well in the September quarter, gaining 11.1%. Over the period, the Index returned 8.5%.

Resources and Industrials had similar rises but a notable feature was how, once again, small companies significantly outperformed large companies. This was especially evident in industrial companies with top 100 industrials returning 3.5% (including dividends) and small industrials returning 8.5%.

Performance Review

Global equity markets had a healthy rally over the quarter with the US S&P500 rising 3.3%, the UK FTSE up 6.1% (so much for the Brexit panic) and Asian markets all strong (HK up over 12%). Commodity markets were mixed with base metals strong, soft commodities weak and oil and gold largely unchanged over the quarter. The Australian Dollar edged up slightly against the Euro and USD to close at US$0.7664.

The August reporting season was less volatile than the interim one in February and on balance there were enough good results through a broad range of industries to maintain our positive view on the growth outlook for the small companies sector.

Positive Contributors: Our best performing stocks for the quarter were generally industrials and pleasingly, came from a diverse group of industries. Heading the list was **Webjet** (+69%) which posted a very healthy full year profit result and announced a deal with Thomas Cook on expanding their global accommodation booking business. Jewellery retailer, **Lovisa** (+51%) also performed well as the company posted a better result from its core Australian operations and outlined plans for expansion into the UK.

Engineering company, **Codan** (+36%) continued to rise with communication device sales rising and a significant contribution from its new range of metal detection equipment. **Service Stream** (+47%) rose strongly on the back of solid profit growth in the 2016 year and the expectation of an excellent forward work book from its NBN infrastructure contracts.

Negative Contributors: Despite our confidence that confectionary producer **Yowie** (-28%) is on track to sharply lift sales in the US, the market was unimpressed with the June quarter figures and the stock slid lower.

Also detracting from performance was lithium producer, **Orocobre** (-22%). After rising significantly over the past six months, the stock retraced in the quarter along with a number of other lithium companies as the spot price for the metal in China came off recent highs. Other detractors for the period were child care company, **G8 Education** (-19%) which suffered from poor figures from its WA operations and low cost recovery in the first half of the year and lease package company, **McMillan Shakespeare** (-14%) that pointed to lower margins in its Queensland operations.

Portfolio Activity

Additions: Travel insurance operator **Cover-More** was added during the quarter on a compelling valuation basis (details below), along with digital services and marketing company, **Melbourne IT** which we see as having a solid growth profile following the bedding down of a number of acquisitions and new blue-chip client contracts coming to fruition. **APN Outdoor** was added to the portfolio after its sharp share price fall following a disappointing interim profit result. We see the outdoor advertising space as continuing to grow strongly over the next few years and the stock price fall provided an ideal entry point at a much more attractive valuation level. We purchased mobile phone operator **Amaysim** during the quarter after their better than expected subscription numbers and operating margins led us to upgrade our valuation.

Exits: **Estia Health** was sold from the portfolio during the quarter after a poor profit result and Government regulatory changes to the aged care industry further compromising their growth profile. This was fortunate timing as the stock has fallen considerably since. Also sold was housing developer **Villa World** on valuation grounds.

At the end of the quarter we had 45 stocks in the portfolio and were holding 3.1% cash.

Performance Attribution^		Key Portfolio Positions^
Top 5 Contributors	Top 5 Detractors	Top 5 Active Holdings
Altium	G8 Education	Aconex
Codan	McMillan Shakespeare	Catapult Group International
Lovisa Holdings	Orocobre	Mayne Pharma Group
Service Stream	Whitehaven Coal*	Shine Corporate
Webjet	Yowie Group	Webjet

^ Alphabetical order. * Denotes stock not held. Attribution is for the 3 months ending 30 September 2016. Top 5 positions are effective 30 September 2016.

Stock in Focus: Cover-More Group (CVO)

CVO is a distributor of Travel Insurance and Assistance Products. The company has historically focussed on Australia/NZ with recent expansion into India, Malaysia, Singapore, China, and most recently the US.

Investment Case Key Questions

1. **Growth Opportunity:** 4 key growth drivers present themselves for CVO and include: expanding distribution channels; geographic expansion; the company's stated goal to grow insurance margins; leveraging off growth in outbound travel. We forecast the company to grow earnings at a compound rate of >15% over the next 3 years.
2. **Management:** We view the new CEO Mike Emmett as highly regarded and his experience places him well-qualified to take the company to its next stage of growth.
3. **Financial Strength:** The Company is conservatively capitalised with 20% net debt to equity at the end of FY16. The company recently raised equity capital to fund the acquisition of Travelex Insurance Services and remains appropriately capitalised to deliver on their growth initiatives.
4. **Risks:** Loss of key contracts; inability to secure underwriting risk; and external shocks such as natural disasters may have a negative impact on outbound travel levels.
5. **Valuation:** On the back of superior growth outlook compared with peer group, we value the company at a resulting target price is $1.61/s and an Assessed Company Valuation return of 17%.