

Flinders Emerging Companies Fund

Monthly Update: July 2022



Performance (after all fees and expenses)	1 Month (%)	3 Months (%)	1 Year (%)	3 Years (% pa)	5 Years (% pa)	Since Inception [^] (% pa)
Flinders Emerging Companies Fund *	10.21%	-11.63%	-17.56%	3.56%	9.99%	9.48%
S&P/ASX Small Ords Accumulation Index	11.43%	-9.94%	-10.93%	2.54%	7.30%	9.14%
Net Value Added *	-1.22%	-1.69%	-6.63%	1.01%	2.69%	0.35%

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

Investment Objective

Exceed S&P/ASX Small Ordinaries Accumulation Index by 3% pa (after-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

Fund Size

\$145.1m

APIR Code

ETL0449AU

M-Funds Availability

Code FEC01

Responsible Entity

Warakirri Asset Management Ltd

Research Ratings

Lonsec: Recommended
Zenith: Recommended

Platform Availability

Macquarie Wrap, HUB24, Netwealth, uXchange, BT Wrap, BT Panorama, AMP, North, Xplore, MLC Wrap, CFS FirstWrap, Powerwrap, Navigator, IOOF, Praemium

Further Information

www.flindersinvest.com.au



- **All change!**
- **Cat: alive or dead?**
- **Warning – reporting season ahead**

The Small Ords Accumulation Index bounced 11.4% in July – its highest gain since April 2020 which followed the Covid melt-down in March that year. Industrials performed slightly better than resources, with healthcare, technology and financials leading. In the market bounce, small caps outperformed large caps (ASX100) by over 6% for the month.

Global markets recovered with the S&P500 rising 9.1% and the Nasdaq 12.3%. European and Asian markets were also firm with the clear exception of China which retreated 4.3% on subdued economic releases and property sector weakness. The bounce in the US was triggered by a reversal in bond yields, and after the sharp rises of May and June where US 10-year yields reached close to 3.5%, weak US domestic data saw them tumble back to almost 2.5% at the end of June – a catalyst for a rally in tech stocks.

Commodities stabilised after also being very weak in May and June, leading to the recovery in mining equities later in the month and the AUD had a late recovery to finish at US\$0.6980.

So, is this the proverbial dead cat bounce or is there some substance to the recovery in small caps? Firstly, it was pretty clear that many stocks had de-rated too aggressively and there were strong valuation signals emerging but at the time, yields were spiking, some corners were calling a domestic recession (and there is one in the US), house prices had begun to fall and energy prices were still moving up. Things are a little different now. Yields have fallen – suggesting that the RBA may settle at the 2.5-3.0% cash rate level rather than higher, employment is still incredibly strong, much of the domestic economy is holding up relatively well and exports are flying – and don't forget that Covid is only now easing. Not wonderful, but certainly not as bad as feared in early June.

A curious set of numbers are the recent consumer and business sentiment and conditions surveys. Both business and consumer sentiment figures are incredibly weak (in fact the consumer is at their third most miserable in 30 years!) but in both cases, spending and conditions look reasonably healthy. While tempting to blame the media and politicians for sentiment, the reality is that both the consumer and business (especially the latter) currently *can* afford to spend and *are* spending – we feel that the market is still reflecting an earnings outlook that is too negative and while we won't repeat an 11.4% monthly rise for some time, there is more left in the recovery.

There will be more clarity on corporate earnings over the next few weeks. Yet another financial year behind us and the results have just started to come through. Cost pressures from labour disruption, energy and other input prices will be a feature, as will higher inventory figures and less predictable cash statements. Companies that have been able to pass on cost rises or efficiently cut costs will be rewarded. We would expect outlook statements to be cautious and guidance to be qualified. It will be very revealing!

Disclaimer and Disclosure

Warakirri Asset Management Ltd ("Warakirri") (ABN 33 057 529 370) (Australian Financial Services Licence Holder No. 246782) is the Responsible Entity for the Flinders Emerging Companies Fund. The material contained in this communication (and all its attachments) is general information only and has been prepared by Flinders Investment Partners Pty Ltd ("Flinders") (ABN 19 604 121 271), a Corporate Authorised Representative of Warakirri. It is not intended to take the place of professional advice and you should not act on any recommendation (if any) made in this communication without first consulting your investment advisor in order to ascertain whether the recommendation (if any) is appropriate, having regard to your investment objectives, financial situation and particular needs. Nothing in this communication shall be construed as a solicitation to buy or sell a security or to engage in or refrain from engaging in any transaction. Flinders believe that the information and advice (if any) contained herein is correct at the time of compilation. However, Flinders and Warakirri provide no representation or warranty that it is accurate, complete, reliable or up to date, nor does Flinders or Warakirri accept any obligation to correct or update the opinions (if any) in it. The opinions (if any) expressed are subject to change without notice. Flinders and Warakirri do not accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of the material contained in this communication. This communication may refer to the past performance of a person, entity or financial product. Past performance is not a reliable indicator of future performance. Investors should obtain the relevant product disclosure statement and consider it before making any decision to invest.

Performance Review

The Fund returned 10.2% in July, 1.2% behind the benchmark which rose 11.4%.

Key Contributors: The recovery in markets during the month certainly helped diversified funds management group, **Pinnacle Investment Management (+42.4%)**. While we considered the stock oversold in recent months, the positive change of sentiment was surprisingly swift. The company has a broad base of affiliate managers spanning numerous asset classes and in early July announced performance fees totalling \$16.4m (net to Pinnacle) for the second half of the financial year – up from \$10.0m in the first half – which highlights the company’s depth of product in weak equity markets.

Also performing strongly was building service provider to the insurance industry, **Johns Lyng Group (31.4%)**. The stock was hit hard in May and June despite re-affirming profit guidance but recovered strongly last month with another flooding incident in Northern NSW being a catalyst. We expect a strong result to be announced in August and solid growth into 2023. As readers would be aware, we have been patient investors in electronic products developer, **Codan (+24.6%)**. The stock has de-rated considerably over the past year despite its global businesses performing well. Earnings have held up reasonably well and we expect further growth in 2023. The communications acquisitions of Zetron and DTC in 2021 are performing well and the metal detection business continues to release new products and enjoy market share gains.

While we been underweight retail stocks for some time, one of our holdings has been overweight women’s garment retailer, **City Chic Collective (+26.8%)**. It has successfully grown market share in both physical stores and online, is well capitalised and well managed. Yes, there is an expectation of increased cost pressure, but we feel that the fear of a sharp downturn in sales and a large inventory overhang are misplaced and were pleased to see the stock recover in July. It was also pleasing to see a recovery in the price of retirement village developer, **Lifestyle Communities (+24.1%)**. It had also been de-rated on the potential impact on its business from higher interest rates, rising construction costs and lower house prices. All potential headwinds, but the company’s upgrade in July to medium term settlements highlighted the strength of the market, their product and management’s ability to control costs and provide a compelling offering.

Key Detractors: Agricultural services company, **Elders (-10.4%)** has been an excellent investment for the Fund over the past few years but the stock took a tumble in July with the identification of Foot & Mouth Disease in Indonesian cattle. We certainly don’t take the threat of the disease making its way to Australia lightly, although all evidence and actions taken by the responsible Government bodies would make it still seem highly unlikely. The cattle market is important to Elders as a selling agent but with so many other parts of their business doing exceptionally well, we feel the 20% retracement over the past two months (with continued supportive climatic conditions) is an over-reaction.

Trans-Tasman childcare operator, **Evolve Education (-18.5%)** had a poor month despite no new news and underlying trading conditions in New Zealand slowly improving. It has been a difficult market for them over the past couple of years with less Government support for the industry than Australia and Covid restrictions that lasted longer. While the near-term results will be challenged, we expect an improvement from all their businesses in the back half of this calendar year. We have mentioned digital payments provider, **EML Payments (-14.6%)** in this section a number of times this year. It has been a frustrating stock for investors. It has some excellent businesses in gift, incentive and re-loadable cards around the world. However, its inability to settle compliance issues with its European regulator (the Central Bank of Ireland) in a timely manner has proved costly, resulted in senior management changes.

Domestic east coast gas producer, **Cooper Energy (-8.2%)** eased over the month despite gas prices remaining high and driving very strong cash flows. We suspect the company is still suffering from stock overhang following the significant \$244m capital raising in June. While the issue was underwritten at 24c per share, it traded below that price in the lead-up to the issue close leading to a shortfall. The acquisition of the Orbost processing plant will be accretive and with the gas price expected to remain at elevated levels for some time, we expect the stock to move higher over the next few months.

Performance Attribution [^]		Key Portfolio Positions [^]
Top 5 Contributors	Top 5 Detractors	Top 5 Active Holdings
City Chic Collective	Cooper Energy	AUB Group
Codan	Elders	Credit Corp
Johns Lyng Group	EML Payments	Codan
Liontown Resources	Evolve Education	Johns Lyng Group
Pinnacle Investment Mgt	Sandfire Resources	Service Stream

[^] Alphabetical order. * Denotes stock not held. Attribution is for the 1 month ending 31st July 2022. Top 5 positions are effective 31st July 2022.

Disclaimer and Disclosure

Warakiri Asset Management Ltd (“Warakiri”) (ABN 33 057 529 370) (Australian Financial Services Licence Holder No. 246782) is the Responsible Entity for the Flinders Emerging Companies Fund. The material contained in this communication (and all its attachments) is general information only and has been prepared by Flinders Investment Partners Pty Ltd (“Flinders”) (ABN 19 604 121 271), a Corporate Authorised Representative of Warakiri. It is not intended to take the place of professional advice and you should not act on any recommendation (if any) made in this communication without first consulting your investment advisor in order to ascertain whether the recommendation (if any) is appropriate, having regard to your investment objectives, financial situation and particular needs. Nothing in this communication shall be construed as a solicitation to buy or sell a security or to engage in or refrain from engaging in any transaction. Flinders believe that the information and advice (if any) contained herein is correct at the time of compilation. However, Flinders and Warakiri provide no representation or warranty that it is accurate, complete, reliable or up to date, nor does Flinders or Warakiri accept any obligation to correct or update the opinions (if any) in it. The opinions (if any) expressed are subject to change without notice. Flinders and Warakiri do not accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of the material contained in this communication. This communication may refer to the past performance of a person, entity or financial product. Past performance is not a reliable indicator of future performance. Investors should obtain the relevant product disclosure statement and consider it before making any decision to invest.