

# Ausbil MicroCap Fund

Quarterly performance update

September 2022

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## Returns<sup>1</sup> as at 30 September 2022

Period	1 month	3 months	6 months	1 year	2 years pa	3 years pa	5 years pa	7 years pa	10 years pa	Since Inception pa <sup>6</sup>
<b>Fund return %</b>	-8.56	4.36	-21.38	-20.03	10.07	9.42	13.06	13.14	17.31	20.40
<b>Benchmark<sup>2</sup> %</b>	-9.83	4.82	-24.63	-18.21	12.92	10.10	10.77	12.09	5.29	4.56
<b>Out/under performance %</b>	1.27	-0.45	3.25	-1.81	-2.85	-0.68	2.29	1.05	12.02	15.84
<b>Reference Index<sup>3</sup> %</b>	-11.20	-0.47	-20.76	-22.56	0.49	-0.80	4.07	7.17	4.58	3.61
<b>Out/under performance %</b>	2.64	4.84	-0.62	2.54	9.58	10.22	8.99	5.97	12.73	16.79

'The macro trumped the micro throughout the month of September, which accelerated the downdraft in equity markets'

## Performance Review

Fund performance for the September quarter was 4.36% (net of fees) versus the benchmark return of 4.82%, as measured by the S&P/ASX Emerging Companies Accumulation Index and the reference index return of -0.47% as measured by the S&P/ASX Small Ordinaries Accumulation Index.

## Fund Review

The macro trumped the micro throughout the month of September, which accelerated the downdraft in equity markets. All eyes were on the Federal Reserve after a series of strong economic data which would likely result in an increasingly hawkish central bank. In a twist, good news suddenly seemed bad for equity markets, all of which indicate that a Fed pivot is not yet on the immediate horizon and the prospect of an economic hard landing will not derail the Fed from reaching their price stability goals.

The Fund marginally underperformed the benchmark in a volatile quarter by -0.45% (net of fees), however it convincingly outperformed the Small Ordinaries Index by 4.84% (net of fees). The Fund benefited from strong earnings results from **Lovisa**, **Data#3** and **Tuas**, and from industrial positions in **PSC Insurance**, **Life360** and **PWR Holdings**. Energy and Materials also supported returns through exposure to rising energy prices and battery materials. The Fund retains its focus on high-quality companies with strong balance sheets, low gearing and recurring earnings that can see through the economic and market uncertainty, and selectively added to positions over the month.

This quarter, the largest positive contributors to performance were **Lovisa**, **Boss Energy** and **Data#3**. Negative contributors included **DGL Group**, **City Chic** and **Aussie Broadband**.

## Key Contributors

**Lovisa** (LOV) rallied 56.4% over the quarter following one of the standout report season results. LOV is in the early stages of a global rollout, with 43 net new stores opening in the second half of the year, and entries into new markets, including Canada and Hong Kong, opening a plethora of growth opportunities. LOV remains the most attractive growth name in our universe with high returns on capital, a 'cookie cutter' store template and a global rollout in its early stages.

**Boss Energy** (BOE) rose 49.2% in the September quarter. Energy outperformed on the backdrop of rising prices in key commodities, including coal and gas, following escalating tensions in the Russia-Ukraine conflict and stockpiling into the European winter. Uranium benefited as the status of nuclear energy grows as a source of low-emissions, dispatchable power, combined with improving sentiment towards reactor extensions and new reactor growth.

**Data#3** (DTL) returned 36.4%. DTL released another consistent earnings result despite a material backlog of delayed hardware revenue. DTL's backlog of hardware revenue was two times larger than last year as demand for networking infrastructure outstrips supply shortages, particularly from key global vendors such as Cisco. DTL is a beneficiary of the underlying growth in larger, digital transformation projects within its enterprise and government customer base, reducing customer exposure risks into an economic slowdown.

## Key Detractors

**DGL Group** (DGL) retraced 45.3% over the quarter after a full-year result that produced weaker than expected cash conversion and a miscommunicated outlook statement. Following an in-depth analysis and review after the result, the Fund added to its position believing there to be 'no-smoking gun' given the weaker cash flow result, which reflected a build of working capital, with the stock now rebasing at much more compelling valuations. An update is anticipated at the AGM in November.

**City Chic** (CCX) fell 28.4%. The market was uncomfortable with management's decision to build additional inventory to mitigate uncertain supply chains into a weakening consumer backdrop. Decisions by founder-led businesses may often run contrary to market expectations, though we expect the market will need to see a consistent reduction of inventory with a stable margin profile before we see any improvement in the outlook for the share price.

**Aussie Broadband** (ABB) fell 31.1% in the September quarter. ABB's forward-looking guidance fell short of market expectations with increased promotional activity by competitors in residential NBN plans detracting from the outlook for subscription growth. Despite the headwinds, ABB continues to take incremental residential share from incumbents and is well positioned to expand into higher margin business and enterprise segments following the acquisition and integration of Over The Wire.

## Outlook

With September's FOMC meeting reinforcing the Fed's commitment to cooling inflation and Chair Powell confirming that growth will need to run below trend to achieve price stability, upcoming earnings announcements will be on close watch for any signs of economic weakness. In Australia, rates are likely to continue increasing in the months ahead, but it is not on a pre-set path. The full impact of recent rate hikes is yet to be reflected in the broader economy, so any material change in policy settings will be data-dependant.

1. Fund returns are net of fees and before taxes.  
2. S&P/ASX Emerging Companies Accumulation Index  
3. S&P/ASX Small Ordinaries Accumulation Index  
4. Top 10 stocks sorted alphabetically.  
5. Date: February 2010.

## Top 10 Stocks<sup>4</sup>

1. 29Metals
2. DGL Group
3. Data#3
4. Imdex
5. Johns Lyng Group
6. Karoon Gas Australia
7. Lifestyle Communities
8. Lovisa
9. Macquarie Telecom Group
10. PSC Insurance Group

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