Flinders Emerging Companies Fund

Monthly Update: November 2021

FLINDERS
Investment Partners

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	-2.06%	-4.88%	14.43%	16.13%	12.15%	13.58%
S&P/ASX Small Ords Accumulation Index	-0.31%	-1.54%	18.44%	13.53%	11.64%	12.86%
Net Value Added	**-1.75%**	**-3.34%**	**-4.01%**	**2.60%**	**0.50%**	**0.72%**

^ 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

$133.9m

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

- **Paying up for very little…**
- **Bond yields back in their box**
- **The strain of new strains**

Market & Outlook

The Small Ords Accumulation Index eased 0.31% in November with resource stocks once again leading industrials. Global equity markets were generally weaker, the Dow down 3.7% for the month but continued strength in technology stocks saw a modest gain in the Nasdaq. Asian markets were particularly weak with Japan and Korea both down over 5%.

Bond yields eased across the globe as growth forecasts were questioned, the US Fed hinted at more tapering and a new South African strain of Covid (Omicron) was detected in a number of different countries. The move in yields also led to recovery in growth and tech stocks after month end that had previously been under pressure. Commodities saw little change with the clear exception of energy with oil prices falling sharply (WTI down 20.8%) on a mixture of Western countries releasing oil reserves, economic growth fears and the Omicron catchall.

While the Small Ords was weaker, there were a number of underlying trends impacting the market that have been in place for the past few months. Stocks associated with battery materials have been on a tear. Yes, the lithium price has been very strong but capitalising current commodity prices is not wise. Two of the world's largest hard-rock lithium mines (Mt Holland and Wodgina – both in WA) will start production in 2022 and a large expansion of Pilbara's Pilgangoora resource will also add to supply. Further significant resources will begin production in 2023. Demand will continue to grow strongly, but at even half the current lithium price, so will supply.

Another feature of the small-cap market is the increasing percentage of the index that is being represented by companies that don't make profits. Mainly in sectors one would anticipate; technology & IT, battery materials and healthcare (biotech to be more specific). Our analysis shows that in FY 2019, 10% of the small-ords index (by market-cap, not number) was made up of companies that were unprofitable. This has leapt to 18% in the forthcoming 2022 financial year – an extraordinary jump. And just as amazing is that since June 30th this year, that a mere 8 of those unprofitable companies represented 48% of the small ordinaries index performance!

We are naturally wary when certain sectors or sub-sectors have dramatic moves and stocks get to unsustainable valuation levels. We've seen it in infant milk formula producers, cannabis companies, buy-now-pay-later and other fin-techs and more recently in online gaming companies. They all come back to earth.

The Flinders portfolio is currently characterised by companies that on aggregate are growing profits at twice the market average forecasts but with a price to earnings ratio discount at the largest level since the fund started in 2015.

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Portfolio

The Fund returned -2.06% in November, 1.75% behind the benchmark which returned -0.31%. November was almost as much about what wasn't in the portfolio as opposed to what was.

Key Contributors: Payments technology and card solutions company, **EML Payments (+22.0%)** bounced following an update as to the discussions with the Central Bank of Ireland (CBI), it's European regulator. The CBI has been investigating EML's European card and payments subsidiary for regulatory compliance and it now seems that the majority of those investigations and new regulatory details are close to finalisation. This is important as the company has significant growth opportunities in re-loadable cards, loyalty programs and other payment systems in Europe. The market had sold down the stock on fears that licences to operate would be lost. This is clearly not the case, and the share price is now recovering to more reflect opportunities in Europe, the US and Australia.

Building services provider, **Johns Lyng Group (+14.8%)** continued to perform well with its underlying services division growing strongly but also a number of significant insurance events hitting the East coast of Australia in November; floods in NSW and QLD and damaging storms in Victoria. While the company doesn't forecast catastrophe work and separates these earnings from underlying services, it continues to prove a consistent source of cash flow. Residential development broadband provider, **Uniti Group (+8.9%)** continues to perform well for the portfolio. The company provided a business update at its AGM during the month which suggested that activity and connections are continuing to grow strongly and customer acquisition is also on track. Uniti continues to win market share from NBN in new developments and is now moving into new commercial developments with success – a significant growth market.

Lithium and nickel producer **IGO Limited (+9.3%)** had another strong month. The company is benefitting from higher commodity prices (both nickel and lithium have risen considerably this year) and it continues to look at growth opportunities through acquisition. IGO is particularly well placed to benefit from the growth in electric vehicles and energy storage with both its major products being a vital part of battery production. And unlike many of its high-flying peers, it already has production of both commodities from world-class, low-cost assets.

Key Detractors: With oil prices under the pump during the month it wasn't surprising that our two energy stocks, **Beach Energy (-15.1%)** and **Cooper Energy (-15.5%)** were weak. This is despite most of Beach's revenues and all of Cooper Energy's revenues coming from the domestic gas market where prices continue to be high. Go figure. We are still very comfortable with the outlook for both companies – they have growth options from their existing asset bases, potential corporate opportunities and longer term, we will continue to see the domestic gas market supported as an adjunct to solar and wind generation growth and as an input to a number of key industrial products. Both stocks have contributed to performance over the past quarter.

Travel company**, Webjet (-13.4%)** tumbled late in the month with the advent of the Omicron strain of the Covid19 virus. A number of countries put into place blanket travel bans and others raised restriction levels. While it is yet to be seen how virulent or dangerous the new strain is, travel related stocks took a hit. At the time of writing, the sector was recovering with less dramatic commentary about the new strain.

And now to the curious situation of five of our top ten detractors (relative) being stocks we don't own. We certainly don't blame the market, but do think it is worth pointing out that the two largest detractors were companies that won't see a dollar of earnings for quite a few years. Battery materials aspirant, **Novonix (+61.5%)** and minerals exploration company, **Chalice Mining (+49.5%)** had a combined market capitalisation of over $9bn at the end of the month – a level that we would suggest contains considerable blue-sky. Lithium producers **Pilbara Minerals (+18.2%)** and **Orocobre (+14.8%)** also negatively impacted relative performance due to their size. We have battery material exposure in companies with more attractive valuation metrics.

Performance Attribution^		Key Portfolio Positions^
Top 5 Contributors	Top 5 Detractors	Top 5 Active Holdings
EML Payments	Beach Energy	Baby Bunting
Johns Lyng Group	Chalice Mining *	Codan
Shine Justice	Cooper Energy	Seven Group Holdings
Uniti Group	Novonix *	Shine Justice
Zip Co *	Pilbara Minerals *	Uniti Group

^ Alphabetical order. * Denotes stock not held.