Flinders Emerging Companies Fund

Monthly Update: July 2021

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	2.08%	4.57%	36.57%	14.03%	11.64%	14.94%
S&P/ASX Small Ords Accumulation Index	0.68%	4.06%	32.30%	9.21%	9.57%	13.00%
Net Value Added	**1.40%**	**0.51%**	**4.27%**	**4.83%**	**2.07%**	**1.93%**

^ 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: RBC Investors Services

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

$109.0m

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, Xplore, CFS FirstWrap, MLC Wrap, Powerwrap, Navigator, IOOF, Praemium

Further Information

www.flindersinvest.com.au

- **Highs for markets and athletes, lows for dealing with Covid…**
- **Impact of lockdowns on small caps**
- **Reporting season and expectations**

Market & Outlook

The Small Ords Accumulation Index rose 0.68% in July with resources strongly outperforming industrials reflecting another strong month for commodities (especially anything found in a battery).

Global equity markets were generally firm with the clear exception those of China and HK. While there were some lacklustre economic releases out of China, it was the CCP interference in the operations and regulation of a number of high-profile tech companies that rattled investors. Stocks such as Tencent, WeChat, Alibaba and Baidu all came under pressure as global investors sold. The HK market lost 9.9% in July and the Shanghai Composite was down 5.4%. Party directives to Chinese industry and business is accelerating and reaching levels that can only stifle economic growth and investment in China over time – a secondary risk to the Australian economy, in addition to the more obvious trade pressures imposed by the CCP.

Reporting season is upon us and as usual, it will be an insight into what's going on at the coalface of corporate Australia. In smaller companies we expect strong results in most sectors – especially those with exposure to consumer spending (hospitality excluded), resources, agriculture, construction and financial services. That covers a significant chunk of the domestic economy so on balance, corporate profit growth (especially the June half) will be exceptionally strong. However, outlook statements will be tempered by the current Covid related lockdowns and the inability for companies to see continuity in their businesses.

Rather than trying to second guess the lockdown vs reopening timelines, our approach remains a focus on companies that can benefit from the underlying stimulatory economic conditions and their own organic growth prospects, and not those that might be whip-sawed by the short term gyrations of state lockdowns. The fund retains a good spread of industry exposures and importantly, it remains at a significant discount to the market – with strong growth. This is vital at a time where some sectors are still experiencing lofty (even speculative) multiples.

We have mentioned over the past few months that M&A activity was expected to pick up. Well, it certainly has. Afterpay/Square has taken the headlines but there have been numerous others and we would expect more in coming months – and capital raisings. With fresh accounts, cheap debt and elevated share prices, companies are well positioned to make acquisitions. It will be a challenge to sift those that can add value for shareholders from those that might not. It is easy to make an accretive acquisition on a PowerPoint presentation – more difficult in practice.

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FLINDERS
Investment Partners

Portfolio

The Fund returned 2.08% in July, 1.40% outperforming the benchmark which returned 0.68%.

Key Contributors: In the past few months we have participated in a number of IPOs that stood out as companies we are happy to invest in – not because we thought there might be a short-term trade. Good market positions, experienced management teams and coming to the market for the right reason – to access growth capital. And attractive valuations to finish the tick sheet. One of those companies, **Trajan Group (+35.4%)** was an excellent contributor to performance in July. Trajan is a Melbourne based developer and manufacturer of specialised consumable components for medical equipment. It has R&D teams and manufacturing in Melbourne and the US and further manufacturing in Malaysia. It has grown organically and by strategic acquisitions and continues to be founder-led. We gained a starting position through the IPO process and bought stock on market in the first days of listing to our required holding.

We mentioned battery related stocks earlier in the report and the sector has done remarkably well. However, some of the stocks are on valuations that imply commodity prices (mainly lithium but also cobalt) that we consider unrealistic despite the enormous growth in electric vehicles and battery storage expected over the next two decades. We currently have three stocks in the portfolio exposed to that industry (to varying degrees)**, IGO (+22.0%), Syrah Resources (+35.7%)** and **Mineral Resources (+17.3%).** All have valuation upside with modest commodity assumptions and in all cases, they are currently *producers* that are growing. And importantly, all are capitalised appropriately for their growth plans – which is rare amongst their peers.

Medical imaging software developer **4DMedical (+25.7%)** had been underperforming in recent months but bounced back strongly in July. The company's unique 'real time' lung scanning technology is undergoing further trials in US hospitals (it is already approved by the FDA and the TGA in Australia). These trials were interrupted late last year and earlier this year by the Covid situation in the US. However, with the increased vaccination rate and lower levels of hospitalisation, trials have recommenced in a number of centres. We expect more positive news flow this half as results are released.

Key Detractors: Online ready to cook meal provider, **Marley Spoon (-30.7%)** fell as it released quarterly figures suggesting that despite strong revenue and subscriber numbers, expenses were running above expectations. This was particularly evident in the US where wage pressures, logistical challenges, and price inflation in other inputs reduced margins. The company has also been investing in new facilities to service the growth opportunities they have – resulting in a period of negative cashflow. However, some of these factors are transitory, and the company has pricing power with its products, so we expect a reversal in the December half, and the company has ample cash availability.

Childcare provider **Evolve Education Group (-13.6%)** also had a difficult month. The company has faced staff availability issues in its New Zealand centres over recent months given border restrictions (impacting availability of qualified educators, which in turn impacts funding for the industry). The Australian business has been faring substantially better but not enough to offset the NZ challenges given the relative size of the operations. We view these challenges to be temporary and expect the company to return to solid growth over the next 12-18 months. Electronic developer and manufacturer, **Codan (-6.5%)** gave back some of its recent gains in July but is still up 107% in the past 12 months. The company continues to be well placed with new products and recent acquisitions supporting growth; the company remains in an upgrade cycle, has a strong balance sheet and valuation upside.

Performance Attribution^		Key Portfolio Positions^
Top 5 Contributors	Top 5 Detractors	Top 5 Active Holdings
4DMedical	Codan	Baby Bunting
IGO	Cooper Energy	Elders
Seven Group Holdings	Evolve Education	EQT Holdings
Syrah Resources	Marley Spoon	SeaLink Travel Group
Trajan Group Holdings	Pilbara Minerals*	Seven Group Holdings

^ Alphabetical order. * Denotes stock not held.

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