Fairview Equity Partners Emerging Companies Fund

31 July 2019

Monthly Report

About the Fund

The Fund invests in an actively managed portfolio of mainly small cap equities listed, or expected to be listed, on the Australian share market.

Investment Objective

The Fund aims to earn a return (after fees) which exceeds the Benchmark over rolling five-year periods.

Benchmark

S&P/ASX Small Ordinaries Accumulation Index ("Benchmark")

Inception Date

8 October 2008

mFund Code

FEP01

APIR Code

ANT0002AU

Minimum Initial Investment

$20,000

Management Fee

1.20% p.a. of the Fund's Net Asset Value.

Performance Fee

20.5% of the Funds quarterly return (after deducting the management fee) in excess of the Benchmark's quarterly return after recouping any prior periods' underperformance in dollar terms multiplied by the Fund's average net asset value over the quarter.

Distribution Frequency

Annually calculated on 30 June.
However, there may be periods in which no distributions are made or the Fund may make additional distributions.

Buy/Sell Spread

+0.30% / -0.30%

Number of Stocks

52

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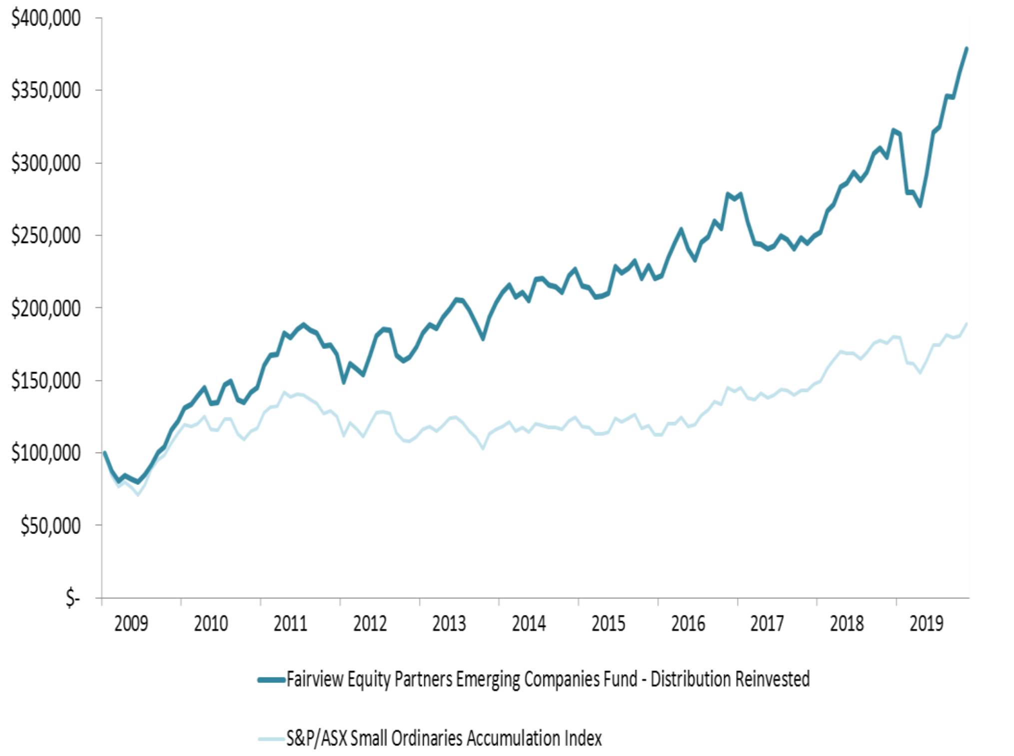
Net Performance

Period	1 month %	3 months %	1 year %	3 years % p.a.	5 years % p.a.	10 years % p.a.	Since inception[1] % p.a.
Fund Return[2]	4.45	9.46	24.47	10.79	11.23	12.58	13.10
Benchmark[3]	4.51	4.15	7.61	9.27	9.18	5.86	6.07
Excess Return	-0.06	5.31	16.86	1.52	2.05	6.72	7.03

[1]Fund inception date: 8 October 2008. [2]Net returns are calculated after deducting management fees and are pre-tax. [3]Benchmark: S&P/ASX Small Ordinaries Accumulation Index. Past performance is not a reliable indicator of future performance. The value of an investment may rise or fall with the changes in the market.

Growth of $100,000 since inception



Performance and Market Outlook

Recent strength continued into July

July is typically a reasonable month for the ASX Small Ordinaries Index to deliver a 4%+ month (4th time in 7 years) and it didn't let investors down. The fund kept up with the buoyant ASX Small Ordinaries Index to a deliver a 4.4% net return. Over the last quarter the fund has delivered 5.3% excess return above the benchmark. The performance of the Fairview Emerging Companies fund (the only fund we run) continues to rank favourably amongst our peers.

Records were reached

During the month the Australian equity markets outperformed most of its global peers. Buoyant iron ore prices, post- Federal election relief and easing (and cheaper) credit availability have helped. The ASX200 was a little late to the party in reaching the pre GFC highs but after 11 years it made it (ASX100 - a month earlier, S&P500 and FTSE100 - 6 years ago). The ASX Small Ordinaries Index remains a long way (30%) from testing the prior November 2017 high, while the Small Resources Index is still 2/3 below its record. Notably, the composition of the ASX Small Ordinaries is vastly different to that period, with lower Energy, Industrials and Utilities sector weights and higher Financials (incl. Property) and IT.

Gold shone again

Continuing June's trend, the persistent backdrop of lowering yields meant investors remained attracted to all things gold (producers, explorers and services). This pushed the monthly outperformance of the ASX Small Resources Index (vs ASX Small Industrials) to levels not seen for ten months (+4.2%). Three of the top 5 best performing Small Caps in July were Gold companies – Dacian Gold (+57% vs -67% in June), Gold Road Resources and Ramelius Resources. Shades of tempered production guidance and rising costs didn't perturb investors. At the time of writing, a member of the Fairview team has polished his boots and attended the Diggers and Dealers Conference in WA scouring for new Resource ideas as well as visiting mine operations.

Can it be sustained?

Undoubtedly the equity market is skittish in the early days of August with a spike in market volatility (which as stockpickers, we love), some lofty valuations, and as anticipated (given the pre Federal election uncertainty), an increasing rate of earnings downgrades (over twice the number of 2%+ EPS downgrades versus July 2018).

With the downgrades continuing

During July the fund avoided all key earning downgrades - Speedcast (share price -46%), Superloop (-36%), Integrated Research (-16%), GUD (-14%) and Adelaide Brighton (-12%), while Bega Cheese (-7%) downgraded early August. While not all these companies might have been considered 'value', it's worth highlighting to our unitholders we perceive value beyond a low PE ratio and a high dividend yield. In our view, these metrics can often indicate a structurally challenged business facing further disappointment. Furthermore, Goldman Sachs research shows growth and value stocks are underperforming equally in the first few days of August. That said, given a disconnect between share prices and the earnings trajectory rate of some companies, we continued to reduce the fund's exposure to select holdings in July.

The stock that surprised us towards month end was Credit Corp (CCP) which provided guidance below the market expectations, but given management's traditional conservatism, analysts revised their numbers only marginally lower. While CCP's share price remains ~5% below the starting point, we think the company is well positioned to win market share in the forthcoming release of consumer debt ledgers from the banks. On the flipside, analysts upgraded Austal's earnings estimates by around 10%. Consistent with our Austal investment thesis, the company is experiencing strong margins from its shipbuilding activities.

A rare gem

Despite reducing the fund's overall Technology exposure we did take a minor position in our first IPO in 2 ½ years - a 26 year old company (they do exist!) called Fineos. Claims management software for the life, accident and health insurance market mightn't sound especially racy for most, but the latent earnings power as the company fully transitions its business to Software as a Service model is attractive (which in our minds, countered the prospect of short term equity market risk preceding a 20 August listing). The team has considered, and rejected, a long list of raising opportunities over recent times but in our opinion, this is a standout.

Reporting season…at the ready!

Finally, while we remain bottom up stockpickers, we observe a long list of external variables – i) the share price reactions of US companies that beat vs missed during the recent Q2 earning season reached extreme levels; ii) US/China trade tensions continue to bubble with iii) escalating global currency ructions (US Fed cut for the 1st time since the GFC, NZ cut by 50bpts); iv) how will a hard Brexit (GBP reached a decade low against the Euro) affect cross border trade?; and v) will the rising Hong Kong hostility spread into broader China social controls? All of these factors point to a lack of definitive company management outlook statements at this month's reporting season.

We expect the spike in share price volatility witnessed in recent reporting seasons to continue, in part due to the increasing prevalence, and at times, unusual stock market influence of passive funds, as well as higher levels of short interest across the sector.

At the time of writing Goldman Sachs has calculated the ASX Small Cap Industrials is trading at a 18% discount to the ASX Large Cap Industrials, 4% below the 19 year average.

Investment Team

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27+ years' Investment Management experience

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