

# Ellerston Australian Small Companies Fund

PERFORMANCE REPORT November 2017

The Ellerston Australian Small Companies Fund employs an active research driven investment approach to identify a portfolio of 30 - 60\* small company securities which aims to deliver returns superior to the S&P/ASX Small Ordinaries Accumulation Index over time.

## Ellerston Australian Small Companies Fund Performance

Return %	Net <sup>^</sup>	Benchmark	Net Alpha	Gross Alpha
1 Month	1.82%	3.91%	-2.09%	-2.03%
3 Months	6.57%	11.60%	-5.03%	-4.83%
Rolling 12 Months	13.47%	20.49%	-7.02%	-5.95%
2 Years p.a.	12.90%	16.95%	-4.05%	-3.04%
3 Years p.a.	11.94%	13.36%	-1.42%	-0.29%
Since Inception p.a.	10.54%	8.99%	1.55%	3.10%

## Ellerston Australian Small Companies Fund Top Holdings

Top 5 Stock holdings as at 30 November 2017	Sector	%
Tassal Group LTD	Consumer Staples	3.36%
Cleanaway Waste Management LTD	Industrials	3.34%
Austal LTD	Industrials	3.13%
Synlait Milk LTD	Consumer Staples	2.91%
Southern Cross Media Group LTD	Consumer Discretionary	2.80%

<sup>^</sup> The net return figure is calculated after fees & expenses. The gross return is calculated before fees & expenses. Past performance is not a reliable indication of future performance

The benchmark is the ASX Small Ordinaries Accumulation Index. The Fund commenced on 10 October 2013.

\*This is the typical number of stocks in the portfolio. The Information Memorandum does allow for 20 - 60 stocks.

## Commentary

The Ellerston Australian Small Companies Fund rose 1.82% in November, underperforming the ASX Small Ordinaries Accumulation Index which rose 3.91%. During the month, the Small Industrials Accumulation Index rose 2.80% whilst the Small Resources Accumulation Index rose 8.09%.

The largest contributors to positive attribution were Speedcast (SDA), Syrah Resources (SYR) and Mineral Deposits (MDL). Speedcast reconfirmed FY17 guidance and management remains confident on achieving organic growth in 2H17 and FY18, on the back of stabilisation in the oil price and increased customer enquiries and activity. Speedcast is also in final negotiations on a few material contracts which could land over the next few months. However little upside from potential organic growth or further acquisition cost savings are reflected in consensus forecasts, and existing consensus earnings multiples remain inexpensive given locked in EPS accretion from recent acquisitions. Syrah rallied significantly as the company completed the initial construction of the Balama graphite project in Mozambique and announced the first production from the project. We initiated a position back in July this year when the share price was \$2.65 and have since seen the share price rally to our initial price target of \$4.25. Mineral Deposits continued its rally for the year on the back of improving prices for mineral sands. Price rises continue to be announced by Iluka and based on the supply/demand outlook it is likely that prices will continue to rise for a couple of years but won't reach the demand destruction levels that Iluka drove Zircon prices to several years ago. On this outlook we remain favourably disposed to the company but are carefully watching the level and pace of new supply potentially coming to market.

The largest detractors from relative returns were Tassal Group (TGR), Autosports Group (ASG) and Macmahon Holdings (MAH). Tassal fell marginally during the month, driven by a fall in international Salmon prices. However, exports are only expected to be 10-20% of total volumes in FY18 and we are about to enter a period of seasonally stronger international pricing. In the domestic market, prices are steady as consumer demand remains strong. This should see all three domestic Salmon players deliver good profit growth for this financial year. Autosports fell on concerns the prestige and luxury segments of the new car market are underperforming. However, we believe the trend towards these segments over mass-market will continue in the medium to long term and the outlook for ASG's "back-end" operations, such as servicing and repairs, is very positive. Autosports have made several acquisitions in the last 12 months which, combined with the maturation of previously established greenfield sites, should underpin growth for the next two years. Macmahon fell marginally for the month after doubling in price this calendar year. The business has recently signed several new contracts which continues to fill out the order book. With successful execution, this should see Macmahon deliver strong earnings growth over the next couple of years and consequently see the share price re-rate further as the market regains confidence in the company after a number of years of poor execution.

## Outlook

Financial year to date the small cap market is up 15%, with Infant formula and Lithium stocks dominating returns. In a rapidly rising market (annualised returns greater than 20%) we would expect to underperform, however, the size of underperformance has been exaggerated by these 2 sectors where we have had zero weighting. Looking forward, we don't see any value in these sectors and are reweighting the portfolio away from resources and growth stocks towards a greater weighting in Value and GARP stocks. There is now a significant PE spread in industrial stocks and many resource stocks are factoring in a significant rise in commodity prices. With an unwinding of QE commencing and interest rates increasing, we feel returns are likely to be lower going forward and are focused on industrials that have had significant de-ratings (where downside is limited) and offer a good sustainable yield which will form a large part of total return. In resources, with a deliberate slowing in Chinese growth, we don't expect significant further price increases and have moved from an overweight position to underweight in the last month, with further reductions likely.

## About the Ellerston Australian Small Companies Fund

The Fund employs an active, research-driven investment approach which seeks to identify a portfolio of smaller company securities with the aim of delivering superior returns to the Benchmark over time.

The Fund will invest in companies that are believed to have the potential to deliver significant upside over the medium term and where there is a reasonable margin of safety to mitigate the downside risk. We will actively manage the positions of the Fund.

Investments will generally be made in companies that have a sound business franchise with an attractive earnings profile, that operate in growth industries and trade at a discount to valuation.

### Fund Facts

Strategy Funds Under Management	\$782 Million
Total number of Stocks	55
Application Price	\$1.1278
Redemption Price	\$1.1222
Inception Date	10 October 2013

## Disclaimer

Returns are unaudited estimates and before fees and expenses and assume distributions have been reinvested. Past performance is not indicative of future performance. This letter does not constitute an offer of any Units in the Fund. This letter does not take into account your investment objectives, financial situation or particular needs. Before making an investment decision about the Fund, persons should read the information memorandum which can be obtained from Ellerston Capital and obtain advice from an appropriate financial adviser. This material has been prepared based on information believed to be accurate at the time of publication. Assumptions and estimates may have been made which may prove not to be accurate. Ellerston Capital undertakes no responsibility to correct any such inaccuracy. Subsequent changes in circumstances may occur at any time and may impact the accuracy of the information. Stock opinions and views expressed in this document are Ellerston Capital's and are not necessarily the views or opinions of the market. To the full extent permitted by law, none of Ellerston Capital, or any member of the Ellerston Capital Limited Group of companies makes any warranty as to the accuracy or completeness of the information in this document and disclaims all liability that may arise due to any information contained in this document being inaccurate, unreliable or incomplete.