

# Ellerston Australian Micro Cap Fund

Performance Report | July 19

## PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	2 Year p.a.	Since Inception (p.a.)
Net <sup>^</sup>	5.69%	10.53%	24.13%	11.85%	14.83%	20.60%
Benchmark*	4.51%	4.15%	15.65%	7.61%	14.85%	13.22%
Alpha	1.18%	6.38%	8.48%	4.24%	-0.02%	7.38%

Source: Ellerston Capital

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

\* S&P/ASX Small Ordinaries Accumulation Index

## COMMENTARY

The Ellerston Micro Cap Fund finished July up 5.69%, outperforming the Small Ordinaries Accumulation Index by 1.18%. Driving the Index was the Materials sector which was up 7.5% for the month on the back of higher iron ore and gold prices. Closely followed by the IT sector which was up 5.6%. Offsetting these gains was the Telco sector which was down 3.0%. Looking at the broader market the ASX 200 finally recovered its pre-GFC high delivering its 7th straight month of gains. The ASX 200 has now delivered 23% return year to date which is its best return since 1991. In July a lot has happened from a macro perspective, with the RBA cutting interest rates by 25bp to 1%. This is the first back to back rate cut since the middle of 2012. We also saw the Business Confidence fall from +7 to +2, giving back some of its post-election bounce we saw in June.

Moving to stocks, July continued to see further downgrades across the street in names like Speedcast, Adelaide Brighton, Cimic and Integrated Research to name a few. We also saw M&A continue to remain a theme with GBST once again receiving additional bids as competition heated up to own the tech financial services play. A stock we spoke of last month and one of our core portfolio holdings Pacific Energy (PEA), also received a takeover offer in July. PEA has entered into a scheme Implementation Deed with QIC. PEA shareholders will receive \$0.975 per share in cash which represented a 35.4% premium to the last close price of PEA pre bid or 50% premium to its 3 month VWAP. The price QIC is paying for PEA works out at an 8.4x EV/EBITDA multiple which is a good outcome for shareholders in our view.

Moving into reporting season in August we believe a number of themes may emerge. We think growth is going to be patchy which will lead to the haves and have not's resulting in a divergence in PE multiples. Consequently, companies benefiting from a lower AUDUSD should see reasonable share price re-ratings as higher earnings flow through. We are also cautious of stocks trading on full multiples. Currently, the Small Ordinaries Index is trading on a one year forward PE of 17.2x which is at an 11.6% premium to its five year average. While some of the movement in the multiple could be contributed to the rise of Small Resources over the past five years, a bulk of the premium in our view is attributed to the multiple expansion in the Small Industrials Index which is trading at a 12.7% premium over the same time period. A consequence of these elevated multiples is any noise surrounding the result may lead to both earnings being downgraded as well as a multiple contraction resulting in a double hit to valuation. Given these dynamics we are very conscious of ensuring any stocks in our portfolio, with full valuations, are appropriately weighted and can clearly demonstrate the growth outlook moving forward.

One stock that has been doing well for us over the last few months is Straker Translation Group (STG). STG operates in the language services industry providing translation platform for content such as operating manuals, legal documents, websites etc. STG has developed a proprietary, cloud based hybrid translation platform which utilises a combination of machine translation technology and crowd sourced pool of freelancers. The combination of STG's tech platform and human translators allows for the translators to work more efficiently which in turn leads to better returns for the company. We have owned STG since its IPO and have been pleased with the progress management have achieved, integrating six acquisitions and beating FY19 prospectus forecasts. We believe given the fact that 83% of STG's revenue is

### Investment Objective

To provide investors with long term capital growth via investing in a portfolio of quality Australian & New Zealand Micro Cap companies. The fund aims to outperform the S&P/ASX Small Ordinaries Accumulation Index over the medium to long term.

### Investment Strategy

The Fund employs an active, research-driven investment approach which seeks to identify and 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 downside risk. Positions are actively managed within the Fund.

### Key Information

Strategy Inception	1 May 2017
Portfolio Manager	David Keelan & Alexandra Clarke
Application Price	\$1.3842
Net Asset Value	\$1.3807
Redemption Price	\$1.3772
Liquidity	Daily
No Stocks	58
Management Fee	1.20%
Performance Fee	20%
Buy/Sell Spread	0.25%/0.25%
Fund FUM	\$106.4 Million
Firm FUM	Over \$5 Billion

recurring and the group still having plenty of cash on its balance sheet to continue rolling up the highly fragmented translation sector, the group should have substantially more growth to come.

Regards



David Keelan



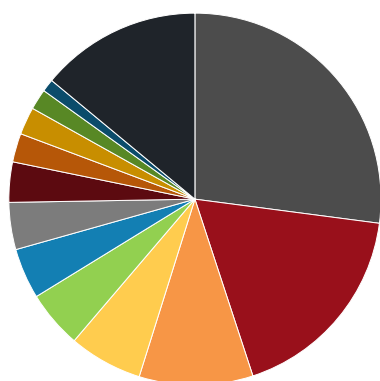
Alexandra Clarke

## PORTFOLIO CHARACTERISTICS

### KEY PORTFOLIO METRICS

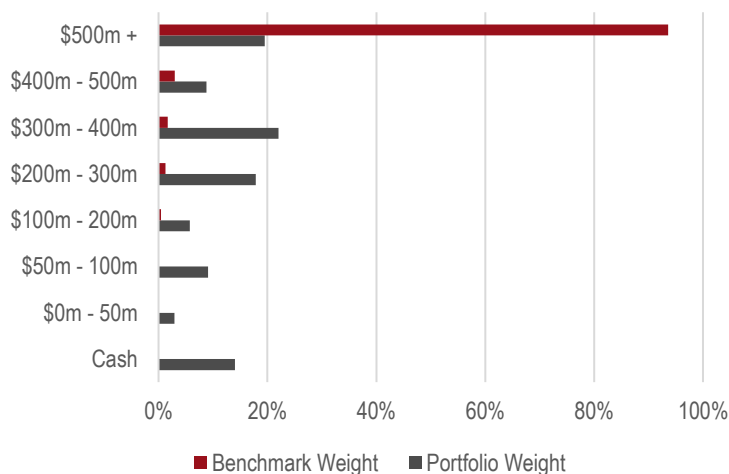
FY20e	Fund	Benchmark
Price/Earnings	14.6x	18.4x
Dividend Yield	2.4%	3.4%
Net Debt/EBITDA	0.0x	1.3x

### SECTOR ALLOCATION



- Information technology, 27.1%
- Industrials, 17.9%
- Financials, 9.9%
- Consumer discretionary, 6.4%
- Materials, 5.0%
- Utilities, 4.4%
- Other, 4.1%
- Consumer staples, 3.5%
- Communication services, 2.5%
- Energy, 2.4%
- Health care, 1.8%
- Real estate, 1.1%
- Cash, 14.0%

### MARKET CAPITALISATION



All holding enquiries should be directed to our registrar, **Link Market Services** on 1800 992 149 or [ellerston@linkmarketservices.com.au](mailto:ellerston@linkmarketservices.com.au)

Should investors have any questions or queries regarding the fund, please contact our **Investor Relations team** on 02 9021 7797 or [info@ellerstoncapital.com](mailto:info@ellerstoncapital.com) or visit us at <https://ellerstoncapital.com/>

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