MARKET MATTERS
INVEST

# MONTHLY REPORT | JULY 2024 | EMERGING COMPANIES

## PORTFOLIO DETAILS

| | |
|---|---|
| Portfolio Name | Emerging Companies |
| Structure | Separately Managed Account |
| Benchmark | S&P/ASX Small Ords Index |
| Management Fee | 0.85% incl GST |
| Platform | OpenInvest |
| Included Assets | Equities |
| Portfolio Managers | James Gerrish & Harrison Watt |
| Annual Performance | 7.46%* |

## OBJECTIVE

The objective of the Market Matters Emerging Companies Portfolio is to provide an active exposure to Australian emerging companies defined as all listed stocks outside the S&P/ASX 100. Returns will primarily be achieved through capital appreciation rather than income with an overall objective of outperformance of the S&P/ASX Small Ordinaries Index over 5 years.

**Inception Date 31.01.2020*

## MARKETS & PERFORMANCE

The Market Matters Emerging Companies Portfolio declined 0.1% in July, underperforming the Small Ordinaries Accumulation Index which increased 3.5%. The portfolio has returned 7.96% for the rolling 12 months and 7.46% per annum since inception, 0.7% per annum above its benchmark.

| PERIOD | 1 MONTH | 3 MONTH | 6 MONTH | 1 YEAR | 2 YEAR PA | 3 YEAR PA | INCEPTION |
|---|---|---|---|---|---|---|---|
| PORTFOLIO % | -0.11 | -3.8 | 0.83 | 7.96 | -0.39 | -3.7 | 7.46 |
| BENCHMARK % | 3.49 | 2 | 2.75 | 9.29 | 4.94 | -0.64 | 6.76 |
| RELATIVE % | -3.6 | -5.8 | -1.92 | -1.33 | -5.33 | -3.06 | 0.7 |

*Benchmark: S&P/ASX Small Ords Accum Index*

More broadly, international markets underperformed the ASX, the MSCI Developed Markets Index rising by (+1.3%), while the S&P 500 increased by (+1.2%) in local currency terms. Australian 10-year government bond yield fell 19 bps over the month to 4.12%, as US yields also decreased, stepping down 32 bps to 4.05%. Commodity prices were mixed in July. Brent Oil fell by US$5.69 to US$80.72/bbl, whilst Iron Ore prices fell by US$4.50 to US$102.00/Mt. By contrast, Gold prices rose by US$95.40 over the month to US$2,426 per ounce after softer-than-expected US inflation data was released.

On a sector basis in Australia, Consumer Discretionary (+9.1%), Property (+6.8%), Financials (+6.3%), Industrials (+5.6%), Communication Services (+5.3%) and Healthcare all outperformed, while Consumer Staples (+4.0%), IT (+0.2%), Materials (-0.1%), Energy (-0.4%) and Utilities (-2.9%) underwhelmed to varying degrees.

## PORTFOLIO POSITIONING

The portfolio held 24 positions at the end of July, as we broadened the underlying exposures, sold some underperformers, and reset for FY25. Harrison Watt was the primary Portfolio Manager since inception, supported by James Gerrish. Harrison has left to broaden his experience in Funds Management overseas, and James is the interim lead on this portfolio, ahead of a new Portfolio Manager starting in September. James will remain a Co-Portfolio Manager ongoing.

We made several changes to the portfolio in July; Selling or reducing weightings in; **SRG Global (SRG)**, **Sandfire Resources (SFR)**, **Austin Engineering (ANG)**, **Pexa Group (PXA)**, **EML Payments (EML)**, & **Bowen Coking Coal (BCB)**.

We initiated positions in; **AIC Mines (A1M)**, **Coronado Global Resources (CRN)**, **Helloworld Travel (HLO)**, **Johns Lyng Group (JLG)**, **Nick Scali (NCK)** & **Zip Co (ZIP)**, and will highlight three positions in this update.

**AIC Mines (A1M)** is an up-and-coming Australian copper producer with a market capitalisation of around $200m, with $74m cash in the bank. While small, it is producing from the Eloise copper mine – a high-grade operating underground mine located in North Queensland currently producing 13,400 tonnes of copper at A5.15/lb and is set to ramp up production meaningfully over the coming years via the expansion of the Eloise processing plant and extension of current life of the operation through the development of another deposit known as Jericho, located 4kms from Eloise. They also have additional exploration assets in New South Wales and WA.

A1M recently raised $57m at 52cps with the placement well sought after – Directors bought ~1.6m, shares in the raise. The timing of the company was impeccable, with copper trading at above US$5/lb, there was strong demand for copper equities. Since then, the copper price has fallen ~17%, and A1M is languishing at 34c, down over 40% from this year's high. Management is key, particularly at this juncture of its life, and Managing Director Aaron Colleran was a founding member of Evolution Mining, managing its business development and investor relations program from inception through to 2018.

| PORTFOLIO STOCKS | |
|---|---|
| NO. OF HOLDINGS | 24 |
| ESTIMATED YIELD (%) | 2.62 |
| TOP 5 POSITIONS (% OF AUM) | 27.14 |
| TOP 10 POSITIONS (% OF AUM) | 47.95 |

| STOCK | CONTRIBUTION (%) |
|---|---|
| AUSTIN ENGINEERING (ANG) | 0.67% |
| REGAL PARTNERS (RPL) | 0.62% |
| RED 5 (RED) | 0.62% |
| SRG GLOBAL (SRG) | 0.51% |
| ZIP CO (ZIP) | 0.26% |

| STOCK | DETRACTION (%) |
|---|---|
| CHRYSOS (C79) | -0.74% |
| CALIX (CXL) | -0.49% |
| AUDINATE (AD8) | -0.39% |
| PALADIN (PDN) | -0.38% |
| AUSSIE BROADBAND (ABB) | -0.37% |

| | JUL | AUG | SEP | OCT | NOV | DEC | JAN | FEB | MAR | APR | MAY | JUN | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **FY25** | -0.11 | | | | | | | | | | | | **-0.11** |
| **FY24** | -1.16 | 6.67 | 1.08 | -7.77 | 4.24 | 5.16 | -1.64 | 4.57 | 3.45 | -1.13 | 0.94 | -4.51 | **9.90** |
| **FY23** | 14.48 | 3.07 | -9.21 | 0.87 | 5.76 | -6.42 | 8.36 | -4.24 | -2.29 | 2.33 | -5.22 | 1.47 | **8.96** |
| **FY22** | 2.97 | 1.17 | 5.91 | 1.13 | 2.19 | -2.47 | -10.29 | -5.93 | 6.68 | -5.19 | -7.80 | -15.25 | **-26.88** |
| **FY21** | 10.92 | 17.19 | -10.89 | 0.63 | 0.58 | 0.57 | -0.86 | 5.91 | -7.10 | 4.38 | -3.81 | 2.37 | **19.89** |
| **FY20** | | | | | | | | -16.09 | -27.07 | 37.98 | 21.26 | 5.66 | **21.74** |
| **CUMULATIVE** | | | | | | | | | | | | | **33.61** |

## PORTFOLIO POSITIONING CONTINUED

The Emerging Companies Portfolio aims to unearth smaller companies with leverage to the themes we like, and copper is one of those.

This is a higher-risk position, more heavily leveraged to the copper price on both the up and downside. However, we like the strategic direction of A1M, with a producing asset and a well-planned exploration and expansion program in play. With cash now in the bank and positive announcements in terms of both production and exploration in recent months, we transitioned from Sandfire Resources (SFR) into A1M for this portfolio only.

**Johns Lyng Group (JLG)** is the number one building repair and restoration insurance business in Australia and ticks a lot of the buzzwords that fund managers like to promote: founder-led, strong organic growth, sector-leading margins, international expansion into a big market, structural tailwinds and a strong balance sheet. All these things are true, yet the stock is down 6% YTD in a rising market and now sits nearly 40% below its all-time high, trading at the lowest PE it's been on in nearly 5 years (25x). This was (and still is) a well-loved stock, and rightly so. The CEO owns almost 50m shares/17.8% of the company, with the top 5 shareholders including The Capital Group (the major seller of FMG on Monday), Soul Patts, Milton and QVG Capital, which equates to a strong share register.

However, the re-rate from the $9.23 high back in mid-2022 has been a result of slowing growth, largely due to lower catastrophes and the stock cycling off an incredible period that saw the share price 5x from 2019. This happens in share markets, where overexuberance gets met with sharp realities – and we now have a quality company back at a level where we think the risk to reward stacks up.

We describe our investment strategy as top-down meets bottom-up, and this stock highlights our process well. At a macro level, we believe the backdrop for the business will improve as interest rates fall, meeting ongoing structural tailwinds of more climate-led catastrophises, rising building costs promoting restorations over new builds, and higher-density living. From a bottom-up perspective, JLG has expanded nicely in North America, which now accounts for ~20% of its revenue, and as their penetration increases in that market – which takes time – the growth in earnings should again re-accelerate.

Our caution previously has been around valuation, which time and the share price have corrected. While it's not cheap, we think there is a good chance that earnings will grow strongly over the next three years.

**Helloworld Travel (HLO)** is a major player in Australian travel, though it doesn't get the airtime of larger rival **Flight Centre (FLT)** and digitally focussed **Webjet (WEB)**. Launched in 2013 after the consolidation of legacy brands Harvey World Travel, Travelscene, Jetset and Travelworld followed by merger with AOT in 2016, Helloworld Travel was born in 2017. It's a $400m business, now growing earnings strongly and is priced at a material discount to the other more well-recognised brands.

Recent strength in ABS travel data prompted MM to revisit HLO, and with the shares trading towards the bottom end of their trading range, we have added HLO to the portfolio.

## PORTFOLIO POSITIONING CONTINUED

ABS numbers for May showed a strong uptick in arrival and departure data, with arrivals up 14% from a year earlier, while departures were up nearly 15%. Provisional data for June implies the same sort of trend, which bodes very well for HLO. From a broader perspective, travel is a discretionary item where cost of living pressures have a negative impact, while the availability and cost of flights are also a key influence. While Australia is not where the US is in terms of interest rates, we are likely to be at some stage over the coming 12 months, providing important cost-of-living relief while airfares are also headed in the right direction (lower).

HLO will report FY24 results on August 23rd, with underlying profit expected to increase to $37m. Looking out to FY25, consensus has underlying profit increasing by another ~20%. At 10.9x FY24 Est earnings, HLO is materially cheaper than FLT (23x). While it doesn't have the scale of FLT, HLO is at an inflexion point for earnings.

Thank you for your ongoing support, we value your trust and look forward to an improving FY25 for small-cap stocks.