

Investment Update

As at 31st March 2019



Spheria Emerging Companies Limited
ACN 621 402 588

Pre-tax net tangible assets⁴
\$2.027

Company⁷ performance p.a.
(since inception)
3.2%

Company Facts

Investment Manager	Spheria Asset Management Pty Limited
ASX Code	SEC
Share price	\$1.725
Inception date	30 November 2017
Listing date	5 December 2017
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Management Fee	1.00% (plus GST) per annum ¹
Performance Fee	20% (plus GST) of the Portfolio's outperformance ²
Market Capitalisation	\$114m

¹ calculated daily and paid at the end of each month in arrears

² against the Benchmark over each 6-month period subject to a high water mark mechanism

Commentary

The Company's pre-tax NTA increased 0.2% in March, adjusted for dividends paid. This represented outperformance of 0.3% compared to the S&P/ASX Small Ordinaries Accumulation Index which decreased by 0.1%

After the strong bounce in January and February the market had a relatively muted month in March. A lot of the key trends which had emerged over the past 18 months re-asserted themselves over the first few months of the year. These being the continued performance of momentum, the relative underperformance of value investing and with M&A continuing to be a key feature of the markets. Whilst we try not to adhere to any particular investment moniker – viewing both growth and value investing as opportunities - we are strong adherents to cash flow investing. That is, we continue to believe longer term valuations derived from reasonably forecastable cashflows are the best way to invest client's money. Whilst this may mean we have some periods of relative under performance we also believe it enables us to derive the best longer-term investment outcomes for clients with – importantly – lower risk than the overall market.

It is for this reason, not for any philosophical reason per se, that we have no exposure to the so called WAAAX stocks (the acronym for Wisetech, Altium, Appen, Afterpay and Xero). Two of these businesses have yet to generate any cashflow (Afterpay and Xero). The others are, in our view, trading at increasingly lofty multiples which make any further re-rating from here a highly risky proposition. It should be stressed here that we are expressing a view on the share prices and what is being imputed into future earnings and cash flows (if they have any) not a negative view on the businesses themselves. Some of these are solid businesses and the innovation and technology they bring to employment in Australia is a good thing. However, you pay a high price for a cheery consensus and right now the consensus is to 'Lets WAAAX lyrical'. The fixation with a segment of the market is not an isolated event of course.

There have been numerous times in the past when the market has become fixated by various sector thematics (viz the tech boom in 99/00, Oil stocks in the 70's and the Nifty Fifty in the 60's and early 70's) to name but a few. In all cases, when momentum takes over and fundamentals are forgotten, the bubble doesn't tend to end too well.

Areas of the market that have instead caught our attention have been the more cyclical parts of the market which have seen their share prices retrace recently. We are finding sectors which are exposed to the housing market (retailers, building materials), the auto sector (auto retail and specialty auto suppliers) and other cyclical areas (discretionary retail and media) are potentially interesting. These sectors have been around for many years and, in contrast to some of the WAAAX stocks, it is relatively easy to see the extent of previous cyclical downturns and calibrate likely mid-cycle earnings. Armed with these facts and the track record of cash flow generation we believe we can selectively invest in the 'unwaaaxed' parts of the market and produce better overall returns from these levels.

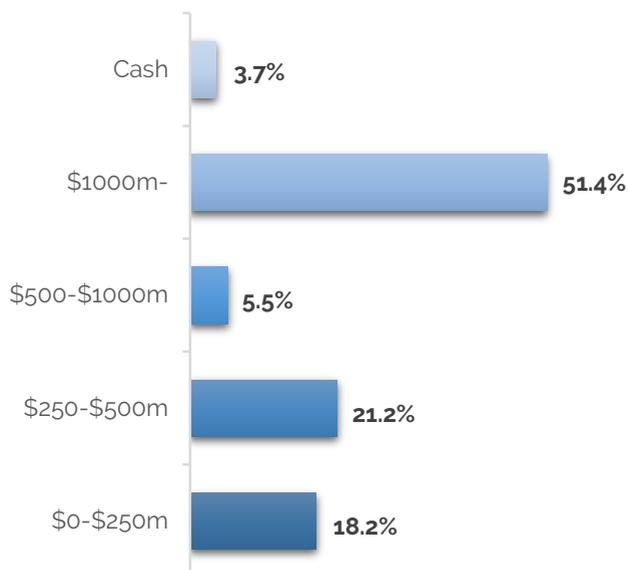
During March the Company benefitted from the performance of Mt Gibson (MGX.ASX, up 14%), Class Ltd (CL1.ASX, up 13%) and Mortgage Choice (MOC.ASX, up 15%). Negative contributors were Platinum Asset Management (PTM.ASX, down 17%), HT&E (HT1.ASX, down 8%) and Wisetech Global (not owned) (WTC.ASX, up 20%). Over the past 12 months despite not owning the WAAAX stocks the Company has outperformed the S&P/ASX Small Ordinaries Accumulation Index. Part of this has been due to the performance attained from a number of stocks which have been the beneficiary of M&A activity (Trade Me (TME.ASX), Navitas (NVT.ASX) and Greencross (GXL.ASX)). In all cases the valuations and cash generating nature of these stocks that piqued our interest also put them in the sweetspot of Private Equity funds or corporate suitors. We continue to find ideas which meet our bottom up investment criteria and sense that M&A is likely to remain a force for the foreseeable future.

Top 5 Holdings

Company Name	% Portfolio
Navitas Limited	6.5
Fletcher Building	5.0
Bega Cheese Ltd	4.8
Class Limited	4.7
Technology One	4.7
Top 5	25.7

Source: Spheria Asset Management

Market Cap Bands



Source: Spheria Asset Management

Net Tangible Assets (NTA)³

Pre-tax NTA ⁴	\$2.027
Post-tax NTA ⁵	\$2.069

³ NTA calculations exclude Deferred Tax Assets relating to capitalised issue cost related balances and carried forward tax losses

⁴ Pre-tax NTA includes tax on realised gains and other earnings, but excludes any provisions for tax on unrealised gains

⁵ Post-tax NTA includes tax on realised and unrealised gains and other earnings

Performance as at 31st March 2019

	1m	3m	6m	1 yr	Inception p.a. ⁶
Company ⁷	0.2%	11.2%	-3.0%	2.5%	3.2%
Benchmark ⁸	-0.1%	12.6%	-2.8%	5.8%	4.4%

Past performance is not a reliable indicator of future performance.

⁶ Inception date is 30th November 2017

⁷ Calculated as movement in Company's pre-tax NTA (which includes tax on realised gains and other earnings, but excludes any provision for tax on unrealised gains), assuming the re-investment of any dividends paid by the company

⁸ Benchmark is the S&P/ASX Small Ordinaries Accumulation Index

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