

## Investment Update

As at 30<sup>th</sup> June 2020



**Spheria Emerging Companies Limited**  
**ACN 621 402 588**

Pre-tax net tangible assets<sup>4</sup>  
**\$1.731**

Company<sup>7</sup> performance p.a.  
(since inception)  
**-2.9%**

## Company Facts

---

<b>Investment Manager</b>	Spheria Asset Management Pty Limited
<b>ASX Code</b>	SEC
<b>Share price</b>	\$1.29
<b>Inception date</b>	30 November 2017
<b>Listing date</b>	5 December 2017
<b>Benchmark</b>	S&P/ASX Small Ordinaries Accumulation Index
<b>Management Fee</b>	1.00% (plus GST) per annum <sup>1</sup>
<b>Performance Fee</b>	20% (plus GST) of the Portfolio's outperformance <sup>2</sup>
<b>Market Capitalisation</b>	\$79.9m

---

<sup>1</sup> calculated daily and paid at the end of each month in arrears

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

## Commentary

The Company's pre-tax NTA decreased 1.5% in June outperforming the S&P/ASX Small Ordinaries Accumulation Index which decreased 2.0%.

Global markets rose again over June, albeit at a less torrid pace than the previous month. While the month saw a significant re-acceleration in COVID-19 transmission rates in the U.S. and a consequent reversal by many U.S. States of their premature re-openings (with the benefit of hindsight), investors looked through these developments to push the S&P500 to within 8.5% of its pre-COVID highs and the NASDAQ to all-time highs. We believe the enthusiasm for stocks is being driven by a realisation that interest rates are likely to remain at depressed levels for an extended period of time and that Governments will have an incentive to essentially monetise some of their COVID-19 induced debt rather than raise taxes during a recovery from the pandemic.

Locally, the Australian broader markets were led up by the banks as they partially reversed a significant period of underperformance on better sentiment towards expected credit losses in the economy albeit the small ordinaries index struggled to keep up. Value cyclicals began the month well but faded as fears of a second wave both internationally and within Victoria built. Momentum stocks, particularly those of a more conceptual nature (i.e. they don't earn a profit) performed strongly as speculative activity by retail participants in the market appeared to hit a new high. The market continued to see capital raisings both by companies hit by COVID-19 (E.g. Qantas, Vicinity, Challenger, Super Retail Group, Investec Australia Property Fund, Arena REIT, APN Convenience Retail, Sky City, Red Hill Education, Viva Leisure) and by tech stocks taking advantage of historically high valuations to do blank cheque raises (E.g. Kogan, Temple & Webster, Openpay). Additionally, gold stocks were very active funding raisings for further exploration spending given the strong performance of the underlying metal and stocks within the sector. The market saw the re-emergence of corporate activity with Infigen (IFN) receiving two separate takeover offers, two gold explorers / developers receiving offers (Cardinal - CDV and Exore - ERX) and Cromwell (CMW) and Opticomm (OPC) receiving offers.

During the month we added to Corporate Travel (CTD), AP Eagers (APE) and Vista Group (VGL). These positions were funded with selling in Adbri (ABC), Platinum (PTM), Blackmores (BKL) and Appen Group (APX).

*Continued on the next page...*

Major contributors to performance were stocks that we owned including:

- Adbri (ABC, +72bps)
- Healius (HLS, +54bps)
- Beacon Lighting (BLX, +28bps)

HLS saw a re-rating post the sale of its troublesome Medical Centres and Dental business for \$500m of enterprise value. This represents 13x EBIT and was a commendable result considering the capital and management intensity of the business. More pertinently it substantially deleverages HLS and allows them to focus on their strong pathology and imaging franchises. BLX had a strong trading update as consumers flocked to stores to undertake DIY projects during COVID-19 restrictions.

Major detractors to performance were:

- Mortgage Choice (MOC, -44bps)
- Bega Cheese (BGA, -44bps)
- Fisher & Paykel (FPH – Not owned, -35bps)

Bega continued to retrace during the month following strong outperformance during the COVID-19 drawdown as investors appeared to use it as a funding source for other positions and in part due to negative sentiment from the catastrophic unwinding of Freedom Foods (FNP – Not owned).

Mortgage Choice appeared to fall on concerns about the sustainability of currently strong levels of application volumes to mortgage brokers. Fisher and Paykel further re-rated following accelerating global COVID-19 cases given it is a COVID-19 beneficiary in its hospital ventilator business.

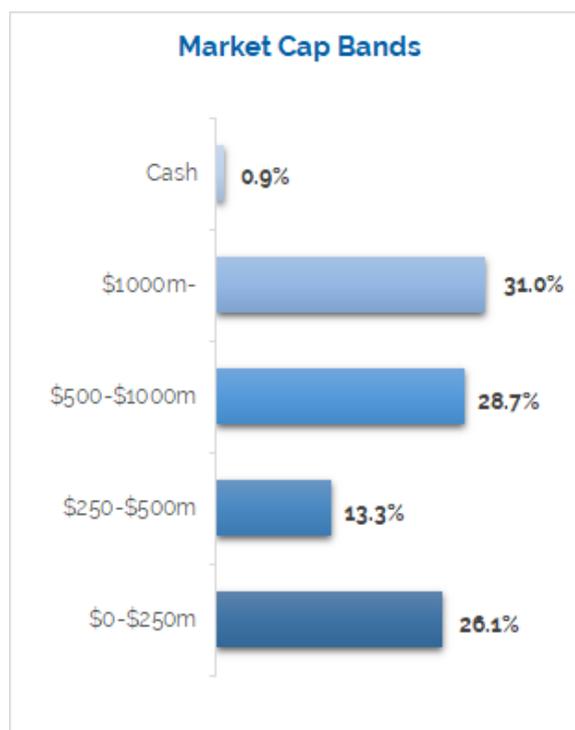
## Outlook

While the market has experienced a meaningful recovery from its lows the manager sees the almost historic levels of multiple divergence as providing some exceptional investment opportunities for those prepared to look through short term earnings uncertainty and/or go against the grain. Equity recapitalisation activity continues to present opportunities for active managers to establish positions in quality companies that have seen cashflow impacted by COVID-19. Additionally, there remain a surprising number of companies that continue to operate profitably and generate cash but that remain on highly depressed multiples, particularly towards the smaller end of the market cap spectrum. On the other hand the manager is increasingly concerned about a narrow subset of very highly rated companies (almost invariably with no track record of free cash generation) that appear to have become completely disconnected from fundamentals, particularly in the technology, fintech and biotech sectors. The manager continues to see better opportunities for relative performance in discovering unpopular but strongly cash generative businesses on attractive through the cycle multiples. While revenue and margins in some of these companies may take some time to recover from the impacts of COVID-19 the manager believes they represent better risk-reward opportunities on balance.

## Top 10 Holdings

Company Name	% Portfolio
Adbri Limited	47
Breville Group Ltd	41
Class Limited	41
City Chic Collective	41
Sims Limited	39
Ht&E Limited	37
Fletcher Building	37
Blackmores Limited	36
Healius	34
Asaleo Care Limited	33
Monadelphous Group	32
<b>Top 10</b>	<b>41.9</b>

Source: Spheria Asset Management



Source: Spheria Asset Management

## Net Tangible Assets (NTA)<sup>3</sup>

<b>Pre-tax NTA<sup>4</sup></b>	\$1.731
<b>Post-tax NTA<sup>5</sup></b>	\$1.864

<sup>3</sup> NTA calculations exclude Deferred Tax Assets relating to capitalised issue cost related balances and income tax losses

<sup>4</sup> Pre-tax NTA includes tax on realised gains/losses and other earnings, but excludes any provisions for tax on unrealised gains/losses

<sup>5</sup> Post-tax NTA includes tax on realised and unrealised gains/losses and other earnings

## Performance as at 30<sup>th</sup> June 2020

	1m	6m	1yr	2yr p.a.	Inception p.a. <sup>6</sup>
<b>Company<sup>7</sup></b>	-1.5%	-15.9%	-12.0%	-6.2%	-2.9%
<b>Benchmark<sup>8</sup></b>	-2.0%	-9.2%	-5.7%	-1.9%	1.4%

Past performance is not a reliable indicator of future performance.

<sup>6</sup> Inception date is 30<sup>th</sup> November 2017

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

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

## Disclaimer

Spheria Asset Management Pty Ltd ABN 42 611 081 326, ('Spheria'), the Corporate Authorised Representative 1240979 of Pinnacle Investment Management Limited (AFSL 322140), is the investment manager of Spheria Emerging Companies Limited ABN 84 621 402 588 ('SEC' or the 'Company'). While SEC and Spheria believe the information contained in this communication is based on reliable information, no warranty is given as to its accuracy and persons relying on this information do so at their own risk. Subject to any liability which cannot be excluded under the relevant laws, Spheria and SEC disclaim all liability to any person relying on the information contained in this communication in respect of any loss or damage (including consequential loss or damage), however caused, which may be suffered or arise directly or indirectly in respect of such information. Any opinions and forecasts reflect the judgment and assumptions of Spheria and its representatives on the basis of information at the date of publication and may later change without notice. Disclosure contained in this communication is for general information only and was prepared for multiple distribution. The information is not intended as a securities recommendation or statement of opinion intended to influence a person or persons in making a decision in relation to investment. The information in this communication has been prepared without taking account of any person's objectives, financial situation or needs. Persons considering action on the basis of information in this communication are to contact their financial adviser for individual advice in the light of their particular circumstances. Past performance is not a reliable indicator of future performance. Unless otherwise specified, all amounts are in Australian Dollars (AUD). Unauthorised use, copying, distribution, replication, posting, transmitting, publication, display, or reproduction in whole or in part of the information contained in this communication is prohibited without obtaining prior written permission from SEC and Spheria.