Bennelong Avoca Emerging Leaders Fund

Monthly performance update

As at 28 February 2019

At a glance

Feature	Fund fact
APIR code	BFL0008AU
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Investment objective	3-5% p.a. above benchmark measured over rolling 5-year periods
Portfolio managers	Jeremy Bendeich/John Campbell
Stock number	32
Fund size	$9.78m
Active stock limit	± 8%
Cash limit	0-10%
Inception date	1 July 2011
Recommended investment period	Long term (five years plus)
Minimum investment	$20,000
Buy/sell spread	+/-0.30%
Entry/exit fees	Nil
Management fee	1.25% p.a. (including GST net of reduced input tax credits) of Net Asset Value of the Fund
Performance fee	17.5% (including GST net of reduced input tax credits) of any amount by which the Fund's investment return (before fees and expenses) is more than 1.25% p.a. greater than the return generated by the S&P/ASX Small Ordinaries Accumulation Index

Performance in review

The S&P/ASX Small Ords Accum. Index (XSOAI) posted a +6.8% return in February 2019 compared to the S&P/ASX 100 Accumulation Index (XTOAI) at +5.9%. XSOAI underperformed XTOAI by -3.7% over the past year and outperformed by +1.0% p.a. over the past three years.

The top five performers in XSOAI in February were BWX Ltd +53.9%, Automotive Holdings +47.9%, Appen Ltd +46.9%, Breville Group +45.2% and Lovisa Holdings +39.2%. The bottom five performers in XSOAI in February were Blackmores Ltd -27.7%, Pact Group -23.2%, Saracen Minerals -23.2%, McMillan Shakespeare -21.0% and Bingo Industries -20.1%.

The Small Resources Accum. Index (XSRAI) rose +5.8% in February vs the Small Industrials Accum. Index (XSIAI) at +7.1%. XSRAI underperformed XSIAI by -8.9% in the year but outperformed by +22.8% p.a. in the three years to 28 February 2019.

Global equities continued their rebound in February. The MSCI World ex-Aust (loc) rose +3.3%, S&P 500 +3.2%, NASDAQ +3.6%, FTSE 100 +2.3%, German DAX +3.1%, French CAC +5.0%, the Nikkei +2.9% and the Shanghai Composite a massive +13.8%.

Global bonds were mixed in February with yields on US 10 years up +8p, UK 10 years +9bp, German 10 years +4bp, JGB yields down -3bps and Australian 10 years -13bp.

The February reporting season was replete with large price moves – often with limited underlying change to business conditions. Automotive Holdings rose 48% due to its balance sheet concerns being ameliorated and, in spite of a poor result, Aveo Group was up 31% on news their strategic review was progressing well, though they also reported a soft result. Breville was up 43% on a solid result which included 15% revenue growth and a positive outlook.

Performance

Timeframe	Fund return	Benchmark	Value added
1 month	6.07%	6.78%	-0.71%
3 months	7.17%	8.01%	-0.83%
1 year	-3.05%	3.48%	-6.53%
3 years p.a.	8.32%	13.44%	-5.12%
5 years p.a.	5.25%	7.73%	-2.49%
Since inception* p.a.	4.51%	4.22%	0.30%

Performance figures are net of fees and gross of any earnings tax. 'Value added' calculation does not use rounded performance figures. *Inception date is 1 July 2011.

The portfolio returned +6.07% in February vs +6.78% for XSOAI, an alpha of -0.71%. Since inception, the portfolio has returned +4.51% vs +4.22% for XSOAI, an alpha of +0.30%.

The top five contributors for February were Aveo +107bp, Webjet +97bp, Seven Group +95bp, Saracen Group +44bp (not held) and GUD Holding +38bp.

The top five detractors for February were Blackmores -185bp, Nufarm -60bp, EQT Holdings -47bp, Mineral Resources -44bp and Altium -42bp (not held).

Outlook and strategy

Exiting unconventional monetary policy has been hard for the Federal Reserve and the ECB. Many market observers are questioning if Central banks have now decided that asset prices and low volatility matter more than employment and inflation. In this new world, we need to accept lower real returns and capital mis-allocation towards long duration assets.

Underwritten by low interest rates, reporting season saw the return of high PE investing. High PE stocks that beat market expectations were rewarded. Low PE stocks that beat market expectations were also rewarded, however considerably less than their high PE peers. Overall, our reporting season scorecard was quite positive with only a large detractor, Blackmores, really a blot on our copybook. What again hurt us was not being invested in high PE tech stocks.

To put performance in context, we have almost kept up with a benchmark that is up over 8% in three months despite not owning a cohort of stocks that have experienced considerable PE expansion. Growth is scarce and discount rates have fallen, favouring these stocks. Consequently, we still tread cautiously around these names. Starting into the new year we were not positioned defensively; our overweights in cyclicals enabled us to catch most of the rebound.

Geopolitical risks continue to dominate, with our portfolio outperforming during 'risk on' periods. Some positions have reacted very positively to the prospect of a trade resolution between China and the USA. Accordingly, we have sold on occasion when fundamentals do not justify the valuation. During reporting season, we were also able to buy some good quality names. Carsales.com, for example, was sold off on short-term cyclical concerns.

We continue to have concerns surrounding the Australian domestic economy. Households are suffering the negative wealth effect of falling house prices. Despite low unemployment, the Reserve Bank appears more likely to cut rates. The market is expecting at least one cut before year end. A lower dollar, coupled with rising sovereign risk, makes investing in stocks with offshore earnings attractive and our position in Webjet reflects this. Australia is addicted to digging holes to extract resources, to build property, and to build infrastructure. With property markets grinding lower, we maintain large overweights to resource extraction and infrastructure plays. Occasionally, we find value in longer-term property plays like Aveo. We are seeing instances of value showing up elsewhere in property related plays but have yet to see attractive entry points.

Largest 10 holdings

Stock name	Portfolio weight
SEVEN GROUP HOLDINGS LIMITED	7.82%
EQUITY TRUSTEES LIMITED	6.36%
AVEO GROUP LIMITED	6.23%
WEBJET LTD	6.06%
GUD HOLDINGS LIMITED	5.75%
AUB GROUP LTD	5.67%
MINERAL RESOURCES LIMITED	4.94%
INDEPENDENCE GROUP NL	4.79%
BLACKMORES LIMITED	4.61%
WORLEYPARSONS LIMITED	4.40%

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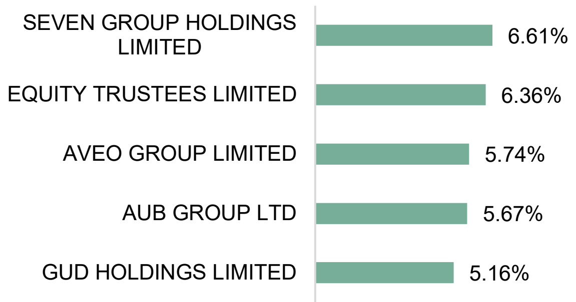
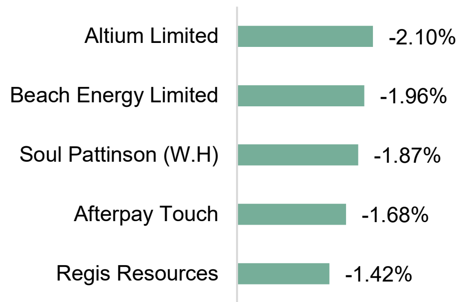
Portfolio analysis

Five largest overweighted stocks



Five largest underweighted stocks



Contact details

For more information, call 1800 895 388 (AU) or 0800 442 304 (NZ) or visit avocaim.com.au

The Fund is managed by Avoca Investment Management, a Bennelong Funds Management boutique.