

## Small Companies Strategy – Investment Newsletter

Performance <i>(As at 31st August 2016)</i>	Month to Date (%)	Quarter to Date (%)	Cal. Year to Date (%)	Fin. Year to Date (%)	Rolling 1yr (%)	Inception (%)
<b>JMFG Small Co. Strategy</b>	<b>-1.75</b>	<b>8.29</b>	<b>14.04</b>	<b>8.29</b>	<b>39.57</b>	<b>65.89</b>
Small Ords Accum. Index	-1.56	6.87	14.28	6.87	26.55	22.80
<b>Outperformance</b>	<b>-0.19</b>	<b>1.42</b>	<b>-0.24</b>	<b>1.42</b>	<b>13.02</b>	<b>43.09</b>

Although the JMFG Small Companies Strategy is generally representative of client portfolios, Individual performance may differ from the results above. These differences can arise due to various issues, some of which may relate to initial timing of investments and cash inflows and outflows. Performance is calculated on TWR basis; non-annualised, excludes fees and the effects of franking credits and tax. Strategy Inception for Performance Data is July 1<sup>st</sup> 2014.

### Month in Review- A review of events that influenced the share market in August.

After a very strong start to the financial year the Australian market took a breather in August with the ASX Small Ordinaries falling 1.56% as the investment community digested a large number of end of financial year results.

As is frequently the case, August was quite a volatile month with a number of company share prices moving up and down more than 20% following the release of their fiscal year 2016 results. Often it is not the results themselves but rather the earnings outlook statements for the next year which draw the most attention.

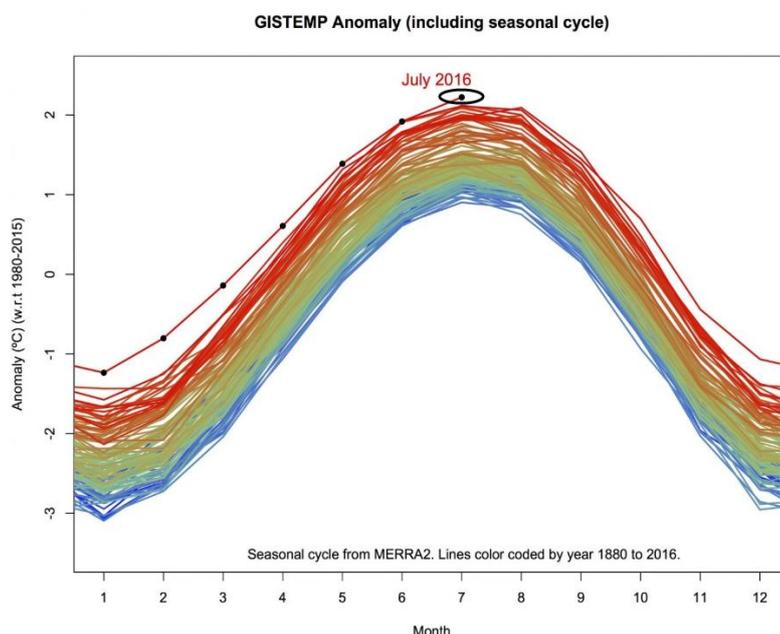
On balance “reporting season” was mildly disappointing with earnings growth still patchy. Once again growth was more evident at the smaller end of the market where the underlying economic environment is less of an influencing factor on the ability of a company to grow its revenues and earnings.

With investors more focused on our domestic equities the impact of global market movements took a back seat until late in the month when Fed Reserve Chair, Janet Yellen, left the door open for an interest rate increase in September. With mixed economic data points in the U.S showing no sustained trend we believe an interest rate rise this calendar year is by no means a certainty.

Amidst the results Woolworths finally announced the sale of its Home Timber and Hardware business to Metcash and the painful closure of its Masters Hardware franchise. One of the more spectacular and well publicised failures in recent corporate history.

After an exhausting reporting season catching up with over 25 companies for one-on-one meetings, attending a number of company presentations and dialling in to numerous conference calls we have a number of stocks on our radar that look appealing from an investment perspective. We look forward to updating you further as we do more work on each.

### Chart of the Month – It’s getting hot in here



During the month NASA confirmed that July 2016 was the hottest month ever recorded. Marking ten consecutive months of record breaking heat across the globe.

Whilst this information has far reaching consequences for the environment we cannot ignore the flow on effects for Australia’s agricultural industry.

For example, California produces 85% of the world’s almonds and has been experiencing five years of drought conditions. With water scarce, nut production has decreased and almond prices have skyrocketed.

This has been of great benefit to local producer, Select Harvests (SHV) but if prices remain at elevated levels we may witness a substitution effect as buyers seek out cheaper almond alternatives such as walnuts.

The agricultural sector has been appealing to us from an investment perspective for a number of years but the NASA data does highlight the fragility and risk of investing in a sector that is so heavily exposed to factors beyond its control.

## Best & Worst Performers for August 2016

JMFG Small Companies Strategy		ASX Small Ordinaries Index	
Best	Worst	Best	Worst
MaxiTRANS - MXI	Datetix - DTX	GWA Group - GWA	1-Page Ltd – 1PG
Wellcom - WLL	Doray Minerals - DRM	Cardno - CDD	APN Outdoor - APO
Mainstream BPO - MAI	Aconex - ACX	Cleanaway - CWY	Wellard - WLD

### Hits & Misses – A summation of the top hits and misses for the month of August.

#### MaxiTRANS – up 29.8% for the month

Trailer manufacturer, MaxiTRANS surprised the market with better than expected trailer sales after flagging weakness in the transport industry earlier in the year. Despite the pressures on the manufacturing sector, MaxiTRANS continues to find further margin efficiencies as it implements a process improvement program across its assembly lines.

#### GWA Group – up 40.2% for the month (Not held)

Household fixtures and fittings supplier, GWA, bounced strongly during the month after posting a 15% increase in profits in FY16. GWA has been a beneficiary of new building activity remaining at historical highs.

#### Datetix Group – down 26.3% for the month

Despite presenting a detailed strategic plan for the business heading into FY17 Datetix suffered from a large shareholder exiting its position. With some of the more illiquid micro-cap companies in the Strategy, large shareholder movements can have heightened impacts on short term prices movements.

#### 1-Page Ltd – down 37.5% for the month (Not held)

As a multiple offender of the worst performing stock in the Small Ords it came as no surprise to see that 1PG has been removed from the Small Ordinaries Index ahead of the September rebalancing.

### Reporting Season Wrap – The Good, The Bad and The Ugly

As alluded to earlier in the newsletter reporting season was volatile with a number of stocks moving greater than 20% following their results release. On balance the disappointments overshadowed the positive surprises with the underlying economy providing no free kicks. Despite the volatility, quality businesses again shone through and below we have noted a few winners and losers from reporting season.

**The Good** - Webjet (WEB) – Continued to confound critics of its business model rallying 26% after delivering record earnings and announcing a strategic partnership with Thomas Cook, one of Europe's leading holiday companies. With bookings up 28% and margins holding steady Webjet is warranting of further analysis.

SRG Ltd - The company formerly known as Structural Systems was finally rewarded for the business transformation strategy undertaken over the last 18 months. The stock rallied 18% after announcing a 53% increase in profits, vindicating the company's strategy to focus on higher margin work. With a diversified revenue base and plenty of cash on the balance sheet we feel comfortable that SRG can continue to deliver strong shareholder returns.

*A typical JMFG company meeting in reporting season...*

**The Bad** - APN Outdoor (APO) – After being one of the market's top performing stocks over the last two years, the announcement of a reduction in forecast growth for FY17 came as a complete surprise and saw the stock sold down 40% in a week.

A rather blunt reminder to management that no matter how strong the business may appear the market does not like negative surprises.



IPH - Patent attorney IPH Ltd, was sold off heavily in August after falling short of the market's revenue expectations. Despite recording 42% earnings per share growth and guiding to further growth in FY17 the shares fell 16% over the month. This was quite disappointing for a business that has previously delivered strong performance for the Strategy. We don't believe anything has occurred within the business to change our view on its fundamental value however we remain watchful for any deterioration in operations.

**The Ugly** - Estia Health (EHE). A number of months ago we discussed the Aged Care sector and our reluctance to invest in it due to a number of factors. Needless to say we were breathing a sigh of relief when we saw Estia Health fall heavily after missing earnings forecasts, announcing the replacement of the CFO in the process. Adding to the pain for investors one of the founders announced his resignation from the Board of Directors two days later and the sale of his 17m shares ( 9% of the company).