

## Small Companies Strategy – Investment Newsletter

Performance <i>(As at 30<sup>th</sup> September 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>2.67</b>	<b>11.18</b>	<b>17.08</b>	<b>11.18</b>	<b>35.34</b>	<b>70.32</b>
Small Ords Accum. Index	1.53	8.50	16.02	8.50	29.16	24.67
<b>Outperformance</b>	<b>1.14</b>	<b>2.68</b>	<b>1.06</b>	<b>2.68</b>	<b>6.18</b>	<b>45.65</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 TWRR 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 September.

Equity markets were mixed in September with the All Ordinaries rising 0.4% and the ASX Small Ordinaries rising 1.53%. Although we are pleased with our continued outperformance, the magnitude of the outperformance over the last 9 months has been less than historical levels. With the Small Ords rising an incredible 29% in the last year we feel there is case of a “rising tide lifting all boats” occurring in the Small Ordinaries at the moment. We believe our approach to targeting high quality growth companies should outperform in the long run.

As widely expected the US Federal Reserve elected to keep rates on hold for another month leaving the door open for a potential raising in December following the US presidential election. With the US now firmly in an interest rate increasing cycle the questions for investors are now, “how quickly will rates rise?” and “can the improvement in the underlying economy offset the increase in borrowing costs?”

With bond yields currently so low the potential for increasing interest rates has already began to impact bond prices and *bond-like* equities such as high yielding real estate investment trusts and infrastructure stocks such as Transurban and Sydney Airport.

On the oil front, OPEC finally agreed to output cuts after months of deliberation, with Saudi Arabia softening its stance against fellow producer Iran, amid continuing weakness in the oil price. On the back of the news, oil prices rose strongly settling around \$50/barrel at the time of writing. Whether this price rise can be sustained remains to be seen with the new output range of 32.5-33 million barrels per day (bpd) set not far below current production levels of 33 million bpd.

And finally, late in the month, German banking powerhouse, Deutsche Bank, came under a spotlight as investors questioned whether its stretched balance sheet could survive a potential \$16 billion settlement with the US Justice Department over an investigation into the selling of mortgage-backed securities. A collapse of Germany’s largest bank would have wide ranging ramifications for global markets, with its share price falling to its lowest level in twenty years.

### Chart of the Month – “Trumped Up, Trickle Down”



Although Republican candidate Donald Trump may have believed he won the first presidential debate, financial markets indicated otherwise pushing the Mexican Peso up to monthly highs during the live telecast.

The Mexican Peso has become the bellwether for investor anxiety due to Trump’s pointed comments on Mexican trade and immigration. With the Mexican Peso breathing easier a number of market indices bounced intraday as millions watched the first of three debates.

Despite not achieving the knockout blow the Democratic Party was hoping for, a number of gaffes and odd digressions from Donald Trump led to most political pundits awarding the points in Hillary Clinton’s favour.

The December election is looming as a pivotal time for markets with a potential Trump victory being viewed as negative for equities. However, not all sectors would be worse off under a Trump presidency with cyber security highlighted as a key issue.

## Best & Worst Performers for September 2016

JMFG Small Companies Strategy		ASX Small Ordinaries Index	
Best	Worst	Best	Worst
SRG Ltd - SRG	Doray Minerals - DRM	SAI Global - SAI	Programmed - PRG
Datetix - DTX	Catapult - CAT	Iselect - ISU	OFX Group - OFX
Base Resources - BSE	Webster - WBA	Alexium - AJX	Doray Minerals - DRM

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

**SRG Ltd** – up 24% for the month.

SRG continued its great run this year with another strong monthly performance. Whilst there was no specific company news a broker report highlighting the undervalued nature of the business appeared to gain some traction in the market pushing it to an 8 year high.

**SAI Global** – up 36% for the month **(Not held)**

SAI Global rose strongly after receiving a takeover offer from Baring Asia. If successful this will be a positive result for shareholders who have had a tough last five years in Australia's leading compliance and risk management business.

**Doray Minerals** – down 19% for the month

Doray had a poor month after releasing further details of its new Deflector mine. With mining ramp up tracking slightly below management's initial expectations the market sold down Doray on fears of a further capital raising. After meeting with management we feel these concerns are misplaced and the company should be able to fund its debt payments through cash flow.

**Programmed** – down 23% for the month **(Not held)**

Programmed fell heavily after reducing earnings forecasts due to a heavier than expected slowdown in its marine businesses following the completion of three large LNG projects.

### Due Diligence – A closer look at a company of interest

**Appen (APX)** – Language technology and crowd delivery

Very few companies can lay claim to having 9 out of the top 10 global technology companies as customers especially when that company is a small, relatively unknown Australian company such as Appen (APX). Whilst Appen may be relatively unknown to most in the market it has been a tremendous success for the JMFG Small Companies Strategy, returning 120% since it was included in the Strategy in 2015.

Appen's Language Resources division provides data for speech-recognition technologies including linguistic materials and analysis, and annotated speech databases.

Although Appen is unable to disclose its customer's specific projects, the growth of voice activated devices is rapid. One only needs to witness the growth of Apple's Siri or Amazon's Echo, to appreciate the growth potential within this business.

The ability of a device to understand a multitude of languages, dialects and tones requires a tremendous amount of raw data which Appen provides through its network of speech specialists and voice data sets.

Appen's other operating division, Content Relevance, is truly a business for the internet age as it utilises Appen's global network of contractors to test or rate web search queries or social media feeds for the relevance of their content.

By utilising Appen's expertise, large search engines, online retailers and social media companies can continually refine their search algorithms to ensure that results obtained correctly matched the search intent.

Given the somewhat private nature of Appen's customer base, forecasting future earnings can be difficult but we feel the strong growth in voice recognition and search will continue for quite some time to come.

### Voice = Gaining Search Share...

USA Android @ 20%...Baidu @ 10%...Bing Taskbar @ 25%

