JM Financial Group

Issue 19: November 2016

Small Companies Strategy – Investment Newsletter

Performance *(As at 30th November 2016)*	Month to Date (%)	Quarter to Date (%)	Cal. Year to Date (%)	Fin. Year to Date (%)	Rolling 1yr (%)	Inception (%)
JMFG Small Co. Strategy	**-0.13**	**-2.05**	**14.68**	**8.90**	**15.68**	**66.83**
Small Ords Accum. Index	-1.19	-5.85	9.23	2.15	13.51	17.37
Outperformance	**1.06**	**3.80**	**5.45**	**6.75**	**2.17**	**49.46**

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 1st 2014.

Month in Review- *A review of events that influenced the share market in November.*

Strange days indeed. These poignant lyrics from John Lennon somewhat encapsulate our views on the rather exceptional month that was November 2016.

After witnessing real estate baron and celebrity TV show host, Donald Trump, stun most political forecasters to win the US Election, the Australian market plummeted, falling 3% intraday as the market reacted savagely to the greatest election surprise in modern history.

As investors around the world braced for the fallout, markets chose to focus on Trump's spending promises to rally 5% across the remainder of the month, with the Dow Jones and NASDAQ setting record highs. Resources were the main driver with zinc, copper, and lead all finishing up nearly 20% across the month. Domestically our market followed suit in a more muted fashion rising 2.5%.

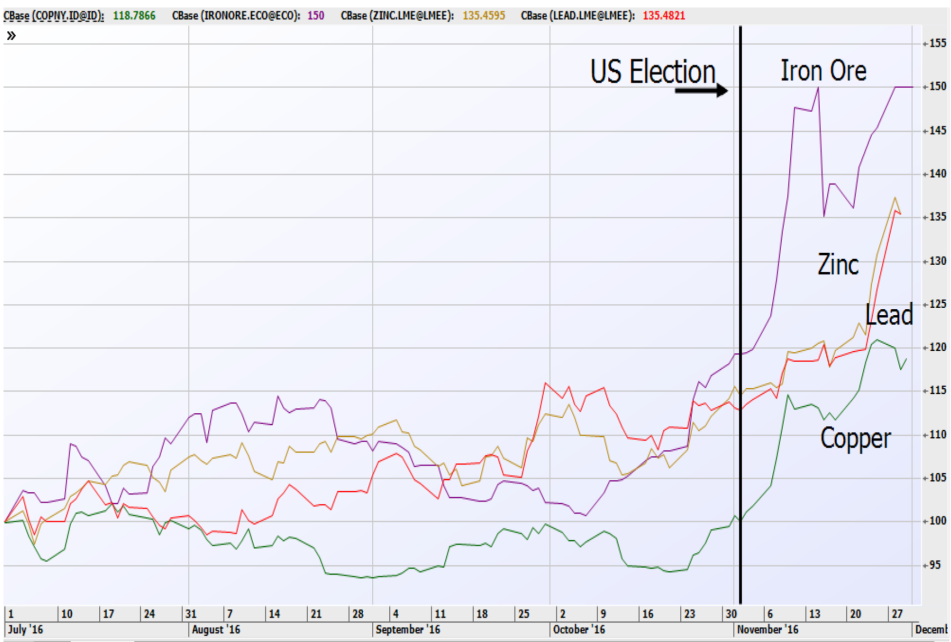
Whilst a 2.5% rise seems relatively standard the composition of this move was quite interesting with a raft of small companies announcing heavy earnings downgrades at their annual general meetings. The Small Ordinaries Index fell 1.2% with the Top 100 companies once again outperforming, returning 3.5% for the month.

To round out a very volatile and somewhat exuberant month, OPEC finally agreed to oil production cuts driving the oil price up a remarkable 8% on the last day of the month as traders took the view that days of $28/barrel of oil are well and truly behind us.

As mentioned previously our domestic market witnessed a number of high profile earnings downgrades from Adairs, Flight Centre, RealEstate.com, Isentia, CSG Group, Vocus, Virtus Health and Scottish Pacific to name a few.

In other company specific news the country's largest poultry producer, Inghams, listed on the stock exchange and building materials producer Boral announced the $2.6 billion acquisition of US peer Headwaters.

Chart of the Month – The return of resources?



Following President Elect Donald Trump's comments on infrastructure spending, the resources market has witnessed an incredible bounce. Investors are now betting that the associated demand for raw materials will push commodity prices out of their post GFC doldrums.

Commodities that are particularly leveraged to construction activity have been the major beneficiaries with iron ore gaining 26%, reaching a level not seen since 2014 and zinc rising 18% to a level not seen since 2008.

Whether the rally in resources can be sustained remains to be seen but with Trump not in office until January 2017 it would appear that the commodity rally could continue throughout the historically buoyant Christmas period.

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Best & Worst Performers for November 2016

JMFG Small Companies Strategy		ASX Small Ordinaries Index	
Best	**Worst**	**Best**	**Worst**
BT Investment Mgmt - BTT	Medical Developments - MVP	The A2 Milk Co. – A2M	Metals X - MLX
Godfreys Group - GFY	St Barbara - SBM	Sims metal Mgmt - SGM	CSG Limited - CSV
Base Resources - BSE	Appen - APX	Galaxy Resources - GXY	Paladin Energy - PDN

Hits & Misses – *A summation of the top hits and misses for the month of November…*

BT Investment Management – up 18% for the month

Investment manager, BTT, bounced strongly during the month after posting stronger than expected FY16 earnings and a positive outlook.

The A2 Milk Company – up 36% **(Not held)**

Although A2M was held in the strategy we sold it earlier in the year due to uncertainty around Chinese customs regulations. A2 have continued to perform well despite this uncertainty and remain the best way to play the Chinese consumer thematic.

Medical Developments – down 16% for the month

Despite posting news of pain relief medication Penthrox being submitted for approval in mainland Europe the stock was puzzlingly weak. We continue to have regular contact with management and remain confident on the long term value of the business.

Metals X – down 53% for the month (**Not held)**

Metals X fell heavily during the month after demerging its Westgold assets into a separately listed vehicle.

Strategy Discussion – *Donald Trump and the return of Populism*

The 2016 US election has proved to be one of the most defining moments in modern political history. A man voted into arguably the most powerful position in the world, with no political experience and only a smattering of support from his Republican Party has redefined the entire political landscape. Trump, to his credit, was able to tap into the underlying anger and disillusionment that has been rippling through "Middle America" since the global financial crisis.

Despite winning the Electoral College vote relatively easily, Hillary Clinton won the popular vote by nearly 2.3 million voters. Never has a losing candidate won the popular vote by such a large margin.

So what does all this mean for financial markets? We have no idea. And neither do any number of financial commentators who have tried to justify the market's incredible 5% move since Trump was announced as President.

It appears that markets have been focussing on Trump's election promises to improve trade terms, "spend bigly" on infrastructure and reduce corporate taxes. Choosing to overlook the numerous misogynist, racist and offensive tweets to focus on his more reconciliatory acceptance speech.

To say we are surprised by the market's enthusiasm for President Trump is an understatement. Although he may be pro-business we have reservations on his ability to fund his election promises without further straining the US's ever burgeoning debt position. Unlike a company, a country can't claim bankruptcy and start again.

Due to our stated strategy of remaining fully invested, clients have benefitted from the "Trump rally" but we have resisted the urge to chase cyclical stocks and resources stocks, preferring to remain somewhat defensive in our stock selection due to the increased volatility a Trump presidency may bring.

Much like our friend to the left, although we are following the market lemmings over the cliff into the Trump unknown we are choosing to do so wearing a life jacket.