Small Companies Strategy – Investment Newsletter

Performance *(As at 31st August 2017)*	Month to Date (%)	Quarter to Date (%)	Cal. Year to Date (%)	Fin. Year to Date (%)	Rolling 1yr (%)	Inception (%)
JMFG Small Co. Strategy	**+2.49**	**-0.30**	**+2.24**	**-0.30**	**-2.02**	**+62.30**
Small Ords Accum. Index	+2.71	+3.06	+4.21	+3.06	+3.54	+26.08
Outperformance	**-0.22**	**-3.36**	**-1.97**	**-3.36**	**-5.56**	**+36.22**

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.

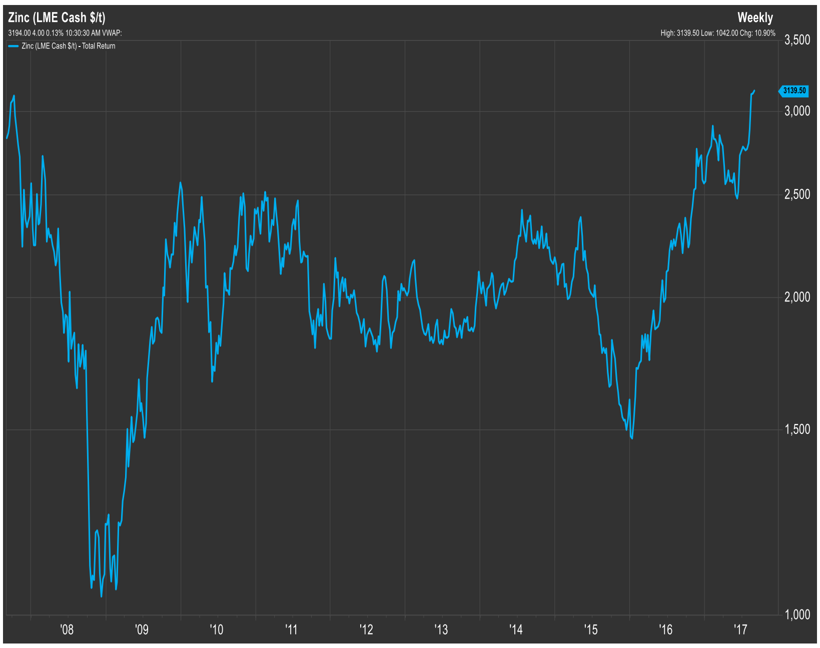
Month in Review- *A review of events that influenced the share market in August.*

The Small Ords Accumulation Index increased by 2.71% for the month, well ahead of the All Ordinaries Accumulation Index, which only increased 0.79%. The JMFG Small Co Strategy marginally underperformed its benchmark, rising 2.49% but outperformed the Small Industrials Index by 1.06%. Strong performance across the resource sector led the market in August with total returns for Materials +4.44%, Metals +5.04%, Golds +11.30%, and Energy +5.74%. The Small Co Strategy, strategically biased toward Industrials, was not far off the pace with strong performances across a number of its technology and financial services investments. Other strong sectors in the month included Consumer Staples +5.33% and Industrials +4.63%. Weak sectors included Telcos -7.37% and Financials -2.19%.

Reporting season was the usual mixed bag of good and poor results and while the Small Companies Strategy had a few disappointments there were no disasters, and a number of very good results and updates were reported. Appen, having upgraded CY17 guidance earlier in the year – from mid-teens EBITDA growth to 40-50% – reached the higher end of the guidance range on their result. The strongest stock rise, +60%, came from Temple & Webster, the online homewares and furniture retailer, which is gaining traction as a legitimate retail operator. In the context of a rising A$ and with 95% of Appen's revenue generated offshore, the update was an underlying upgrade. Appen's shares increased 12% over the month. Other strong performers in the portfolio, on the back of good results, included SRG Group +17%, Class Ltd +15%, EML Payments +14%, and GTN Ltd, which reported on the 31st up +5%, and continued its rally into September.

During the month, we reduced holdings in Base Resources and Temple & Webster on share price strength. We exited Mayne Pharma and Technology One, the former due to a weakening generics business in the US and the latter on a PER over 30x and moderating growth. We introduced New Century Zinc into the portfolio on improving zinc economics and reopening an existing mine with all infrastructure in place. Aeon Metals was opportunistically traded in and out of the portfolio on an attractive capital raising price.

Chart of the Month – Zinc Prices US$/t



The zinc price has experienced a significant recovery in the past two years, in part reflecting production closures, along with growing demand on the back of global economic growth. China, producing over 40% of global annual zinc, has cut production by 10% to 4,500,000t. The largest cut has come from Australia where production has halved to 850,000mt, largely due to 2016 closure of the Century Zinc mine, which had produced up to 500,000t annually.

Under the proposal to reopen Century Zinc, the tailings processing proposal will see less than 200,000t added back to annual production. As capacity comes on we would expect moderation in the zinc price with a realistic long term price range of US$2,000-2,500/t based on zinc prices over the past decade.

Note the volatility with prices falling to abnormally low levels around US$1,100/t during the GFC and close to US$1,500/t at the end of CY15 early CY16, a period of weaker global growth.

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Best & Worst Performers for August 2017

JMFG Small Companies Strategy		ASX Small Ordinaries Index	
Best	**Worst**	**Best**	**Worst**
Temple & Webster - TPW	Netcomm Wireless - NTC	Starpharma Holdings - SPL	CSG - CSV
SRG - SRG	Catapult Group International - CAT	Highfield Resources - HFR	GBST Holdings - GBT
Class Ltd – CL1	Love Group - LVE	Blackmores - BKL	Mayne Pharma - MYX

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

Temple & Webster – up 60.0% for the month

A promising second half result demonstrating a combination of revenue growth and cost reductions for a significant improvement in the operating loss rate for this start-up online retail operator. While it still has a long path ahead, the business appears to be gaining traction.

Starpharma Holdings – up 36.8% **(Not held)**

Successful phase 3 trialling of its VivaGel products comes on the back of its $35m Agrochemicals business sale announced in July. Commercialisation of the VivaGel product range is expected through FY18.

Netcomm Wireless – down 16.8% for the month

A disappointing month with no negative news in the FY17 result and confirmation of strong growth to emerge in FY18 on the back of previously announced contract wins.

CSG – down 43.5% for the month (**Not held)**

A print and communication services business that reported disappointing results, an impairment charge of $55m and cancellation of its full year dividend to preserve capital for investment. In addition flat EBITDA growth didn't inspire the market.

Due Diligence – *a closer look at a stock of interest*

EML Payments (EML) – A Card For Everything

EML provides payment solutions for businesses serving other businesses and consumers through a range of different card offerings. These include:

- Supplier Payment Cards providing full line payment services including virtual, automated clearing house, and eCheck.
- Payout Cards for gaming, commission payouts, and government disbursement and healthcare reimbursements.
- Incentive & Reward Cards commonly used by retail organisations as loyalty programs, promotional cards, and mobile apps to pay, earn, and redeem.
- Gift Cards for shopping centres, retailers, precincts, or a group of specified retailers/merchants etc

EML Payments has gained significant traction over the past five years, developing and expanding its card payment solutions across retail, gaming, and business to business segments. Its success can be measured by the increase in Gross Debit Value held across its card offerings.

Gross Debit Value has grown from moderate levels in FY13 to $1b in FY16 and substantially in FY17 to $4.4b. This has translated into revenue generation expanding to $58m in FY17, up from $23m in FY16 and EBITDA growing from just above $5m in FY16 to $14.5m in FY17.

EML operates in Australia, North America, and Europe, and has the prospect of significant growth, with expanding acceptance and the fact that EML holds only a small share of the potential markets in each region. North America is EML's largest market with around 80% of Gross Debit Value and 65% of revenue generated from North America in FY17. Australia generated around 15% of GDV and 17% of revenue for EML.