JM Financial Group

Issue 48: April 2019

Small Companies Strategy – Investment Newsletter

Performance *(As at 30th April 2019)*	**Month (%)**	**Rolling 3mths (%)**	**Rolling 1yr (%)**	**Rolling 3yrs (%)**	**Inception (%)**
JMFG Small Companies Strategy	**+7.07**	**+12.15**	**+7.38**	**+47.67**	**+106.80**
Small Ords Accumulation Index	+4.11	+11.04	+7.18	+39.70	+55.47
Outperformance	**+2.96**	**+1.11**	**+0.20**	**+7.97**	**+51.33**

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 a TWRR basis; non-annualised, and includes fees (post 1 Jan 17) and taxes. Strategy Inception for Performance Data is July 1st 2014.

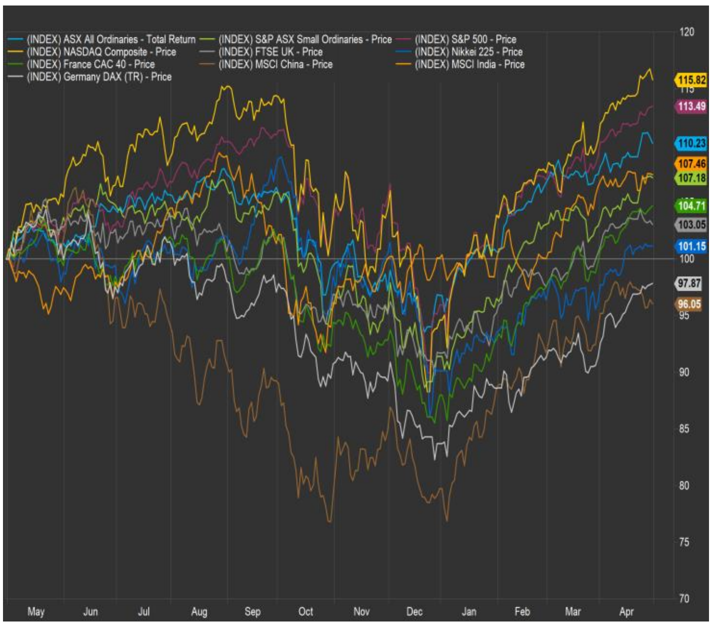
Month in Review – *A review of events that influenced the share market and portfolio in April*

The ASX Small Ordinaries Accumulation Index had a strong month, rising by 4.11%. The JMFG strategy comfortably beat the index for the month, rising 7.07%, outperforming by 2.96%. It was particularly pleasing to see a number of our investments at the smaller end of the market capitalisation scale start to generate significant returns. Some of these investments had been testing over the past 12 months, but staying close to management and their strategies helped us maintain the faith and for some we still see significant upside potential. The ASX Small Industrials rallied 6.30% while the ASX Small Resources fell 4.17%. Strongest sectors during the month included I.T. and Consumer Staples, each rising 7.3%, Consumer Discretion rising 5.0% and Financials +4.4%. Weakest sectors included Property Trusts -2.6%, Materials -2.0% and Utilities -0.5%.

Our best stocks for the month were all technology based with fintech Selfwealth rising 63%, medical tech companies Polynovo +38% and Mach7 +35% and imagery technology companies SenSen +29% and Nearmap +23%. Weakest stocks included Praemium Ltd -25%, Base Resources -11% and The Citadel Group -7%. Sector valuation continues to march onward with the ASX Small Ords 12-month forward PER, as per *Factset* consensus data, now trading at a virtually unprecedented high of 18.4x PER. We see this as a function of the low interest rate environment and the increasing size of highly scalable technology stocks now comprising the index. Nevertheless we tread cautiously.

We added three new stocks into the portfolio during the month. Superloop and McMillan Shakespeare were added on price weakness, the former in our view having strategic asset value and the latter simply becoming cheap while offering system growth but continuing to face cyclical headwinds for the time being. We also added Altium for its long term growth potential and highly scalable business model. We exited GUD Holdings and reduced holdings across a number of stocks where we saw significant recent price strength including Temple & Webster, Appen, Polynovo, Medical Developments and Cleanaway. We added to holdings in St Barbara, Rural Funds Group and Infomedia.

Chart of the Month – Equity Markets



In this month's chart, we compare a selection of equity market returns, indexed from 30th April 2018 through to 30th April 2019. Over that 12 month period, on a total returns basis, which includes the accumulation of dividend and capital returns, the Australian market has performed quite well in its own right, and against most other markets.

The US S&P 500 (yellow) and NASDAQ (purple) composite performed better than the Australian market (light blue), rising by 15.8% and 13.5% respectively, compared with the Australian market which rose 10.2%. The ASX Small Ordinaries (light green) by comparison rose 7.2%.

The Chinese (brown) and German (white) markets were in negative territory, falling between 2-4%. The Japanese (dark blue), French (dark green) and UK (grey) markets were between 1-5% ahead for the 12 month period.

From an Australian market perspective there were two sectors that stood out over the 12 months. The high growth, high P/E Ratio IT sector increased 33%, with many companies finding attractive niches in the IT space. The Property Trust sector, offering attractive yields and moderate growth also attracted funds, aided by ongoing low interest rates both in Australia and globally.

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Best & Worst Performers for April 2019

JMFG Small Companies Strategy		ASX Small Ordinaries Index	
Best	**Worst**	**Best**	**Worst**
SelfWealth – SWF	Praemium – PPS	Eclipx Group – ECX	Praemium – PPS
Polynovo – PNV	Base Resources – BSE	Kogan.Com – KGN	Pilbara Minerals – PLS
Mach7 Technologies – M7T	The Citadel Group – CGL	Megaport – MP1	Galaxy Resources – GXY

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

SelfWealth (SWF) – up 62.5% for the month

A strong recovery after announcing the completion of a capital raise in March and providing a trading update in April which outlined 30% growth in trading volume, growth in active traders of 23% and a 22% jump in client cash balances to $75m.

Eclipx Group (ECX) – up 58.6% for the month (Not held)

Eclipx previously fell sharply after McMillan Shakespeare and Eclipx agreed to terminate the Scheme Implementation Agreement with a full reimbursement of $8m in relation to costs incurred by McMillan Shakespeare, this rise followed on easing of selling pressure.

Praemium (PPS) – down 24.6% for the month

Praemium fell after one of its major clients, ANZ Private, informed the company that it had selected an alternative supplier. The account generated $4m for Praemium in FY18, around 8% of its annual revenue.

Pilbara Minerals (PLS) – down 22.8% for the month (Not held)

A gradual decline occurred over the month despite confirmation of no change in either production targets or forecast financial information. The share price decline reversed immediately after month-end when Wesfarmers announced a proposal to acquire another lithium producer in Kidman Resources.

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

Breville Group (AIA)

Breville Group was added to the portfolio prior to the release of its first half fiscal year 19 result. The addition to the portfolio followed a 25% share price decline in the preceding months, which in our opinion made the stock look relatively cheap against an increasingly expensive market. The company reported a strong first half result with net profit after tax increasing 20% on a 15% rise in revenue. Since inclusion, the stock has appreciated by over 60% and paid a dividend. We now grapple with whether the stock has run too far, with its current price to earnings ratio based on consensus data at 36x FY19, and 32x FY20 forecast earnings.

Breville is an iconic brand in the Australian market, of which most Australian households would have some degree of recognition. It is also a major international success story, delivering kitchen products to over 50 countries. In May 2013 it launched a range of 17 premium designed and developed products into the UK under the *Sage* brand name, sitting alongside its premium *Breville* branded products. It offers more affordable branded products in Australia and New Zealand under the *Kambrook* range, encompassing kitchen appliances as well as living room, laundry and bedroom products such as irons, vacuums, heaters, electrical blankets and fans. Breville offers a mid-priced value brand under the *Ronson* name in the Australian market.

Breville has developed a strategy of creating more product and distributing through a broader geographic footprint with European sales starting to represent a meaningful proportion of total sales. Revised branding and distribution strategies is now realising faster product uptake into new European markets with sales levels in Germany some 3.5 years ahead of the experience following entry into the UK in 2013. Breville plans to enter Spain in FY20.

Product Development, Distribution Strategy & Geographic Diversification Drive Growth

AUDm	GLOBAL PRODUCT SEGMENT REVENUE			
	1H19	1H18	% Chng $A	% Chng CC*
North America	214.9	188.1	14.2%	7.1%
Australia and New Zealand (ANZ)	74.1	68.7	7.9%	7.6%
Europe**	51.4	36.8	39.5%	32.0%
Rest of World	15.7	16.4	(4.3)%	(11.2)%
TOTAL	356.1	310.1	14.8%	9.2%

*CC - Constant Currency

** Europe includes all sales made to European customers. The segment includes Turkey, but excludes Russia. Prior period has been restated on a consistent basis to allow compari