The University of Queensland Business School

The University of Queensland Australia

Create Change

Student Managed Investment Fund May 2020 Update

May 2020 Fund Update

Introducing Zion Capital

May marked the end of Team Hadrian's management of the portfolio and the beginning of Zion Capital's 6-month tenure. We are grateful for the opportunity to manage the fund and look forward to maintaining the high performance of the portfolio. Zion Capital looks to invest in high quality, growing companies exposed to long-term structural tailwinds at an attractive price. To us, growth in revenues and earnings is the best catalyst for generating shareholder returns in the long run.

During May, Zion Capital and the SMIF student community also had the opportunity to hear from numerous industry mentors including Ben Griffiths and Tim Serjeant from Eley Griffiths Group and Joshua Derrington and Chris Scarpato from Alvia Asset Partners. We are extremely grateful for their insightful feedback and look forward to their continued guidance for the SMIF community.

Fund Review

The portfolio returned 7.9% during the month of May compared to the benchmark All Ordinaries Accumulation Index return of 5.0%, representing an outperformance of 2.9%.

With the markets rebounding sharply following the March sell off, the fund was well positioned in the consumer discretionary and materials sector which contributed over half of the fund's returns. Top performers for the fund included Breville Group (ASX:BRG), City Chic Collective (ASX:CCX) and Qube Holdings (ASX:QUB), which returned 27.3%, 24.0%, and 22.6%, respectively, over the month of May. Only four positions produced a negative return including CSL Limited (ASX:CSL), Sydney Airport (ASX:SYD), Cooper Energy (ASX:COE), and Woolworths Group (ASX:WOW) with returns of -10.7%, -7.1%, -3.5%, and -1.2%, respectively.

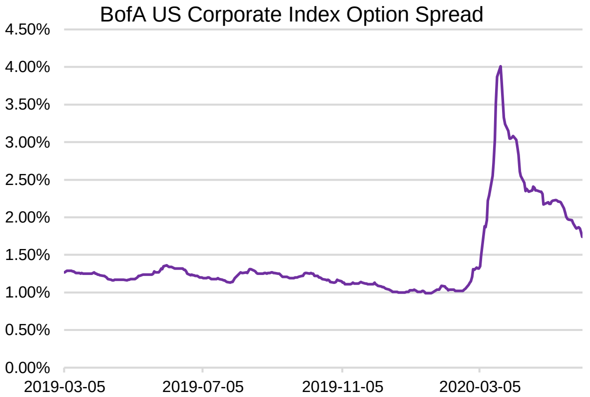
Since taking over management of the portfolio earlier in the month, Zion Capital has added four high quality ex-ASX300 positions into the portfolio to diversify into the small-cap sector. These include City Chic Collective (ASX:CCX), PWR Holdings (ASX:PWH), Integral Diagnostics (ASX:IDX) and Johns Lyng Group (ASX:JLG) all of which are set to benefit from strong tailwinds and lead their respective markets in line with our Zion investment philosophy.

Furthermore, the concentration of the top 5 positions within the fund was reduced from 37.3% to 28.3% in order to diversify the fund and reduce major exposures. This change in fund positioning was further emphasised in our discussions with Ben Griffiths (Eley Griffiths Group). Hence, the team sold down Chorus (ASX:CNU), Macquarie Group (ASX:MQG), ResMed (ASX:RMD), and Appen (ASX:APX), though CNU, MQG and RMD still remain within the fund's top 4 positions due to our high conviction in their respective returns. The total number of positions in the portfolio has also increased to 27 holdings. Additionally, following our discussions with Tim Serjeant from Eley Griffiths Group, we will be looking to further diversify our gold exposure in the fund and have taken on his comments relating to selecting attractive positions in the sector.

Market Update

The Australian All Ordinaries Index delivered a positive return of 4.9% in the month of May as investor confidence continued to lift, driven largely by the early removal of social restrictions and the continued global ultra-dovish policy response from central banks. Australian resources companies were among the best performers in May (11.32% return) as BHP, RIO and FMG rallied on the back of higher spot iron-ore prices driven by expected supply-side issues in Brazil. The big four banks experienced a strong rally in the last week of May that resulted in the ASX200 banks index rising 16.5%. The Aussie dollar has continued to rally in the risk-on environment, reaching 0.66 AUD/USD, up 15% from the March lows.

Looking overseas, the S&P 500 delivered a positive return of 7.4% in the month of May, largely on the back of continued strength in the FAANG+ collective. This strength in the equity market was upheld in the US primary bond market, with Amazon issuing $1B of 3-year notes at 20bps above the 3-Year Treasury, the lowest yield for a corporate issuance in the history of the US primary markets. This follows a month of large US corporate bond issuance as companies look to bolster their balance sheet with attractive yield offerings as spreads approach pre-COVID levels following the Feds unprecedented policy response.



Source: Federal Reserve Economic Data

Looking into June, the SMIF team believes there are three key risks that market appears to be overlooking. Firstly, the market seems to be discounting any continued escalation surrounding China-US trade tensions, which have the ability to materially damage global growth prospects coming out of impending recessionary environment. Secondly, markets appear to have shrugged off any potential for a second wave in COVID-19 cases, particularly given the increase in protest activities across the entirety of the US. Lastly, current market levels imply a V-shaped recovery in furloughed positions and little additional job losses due to the recession rather than the pandemic. Given the large variance of professional estimates on upcoming US non-farm payroll and Australian employment data, there is room for serious volatility in equity markets as this data is released over the coming weeks and months.

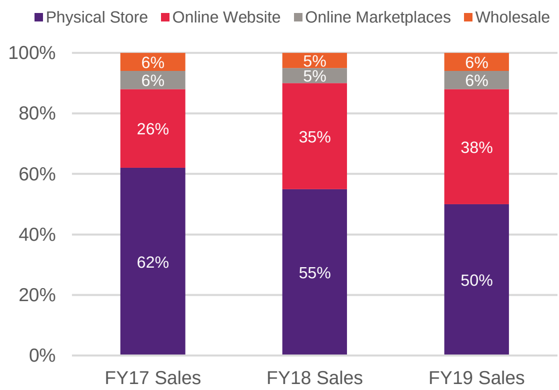
While as a PM team we don't see it within our scope to give predictions on these matters, it is integral to monitor these risks in order to effectively position the portfolio for long-term success.

Stock Spotlight

City Chic Collective Ltd (ASX:CCX)

City Chic Collective is a plus-size women's clothing retailer with global exposure and a portfolio of four brands including *city chic*, a fashion forward mid-market offering, *CCX*, with online retailing offers youth casual styles, *Avenue*, the U.S. online conservative segment and *Hips & Curves* which is the second U.S. acquisition offering playwear, intimates and lifestyle clothing.

1HFY20 results were released to market on 20 February 2020 reflecting the success of CCX omni-channel retail model. This reported sales revenue of $104.8 million, a 39% increase from the prior 1H FY19 period and 11.3% comparative sales growth (excluding online, marketplace and acquisitions). More notably, Online revenue grew 101.5% from the comparative period. Further, online sales penetration increased 32.5% from 40% to 53% of sales from the prior period.



Source: Company Reporting

This highlights the success of CCX's organic growth which has been complemented through acquisitions of Avenue and Hips & Curves. Gross margin decreased from 60.4% to 54.2% from the prior period 2HFY20. This was due to the lower gross margin of the acquired businesses while in-store gross margins were maintained. The update revealed the strategic focus of improving the gross margins on the acquired businesses through increasing average sell price and migrating consumers to online channels.

After temporarily closing Australian and New Zealand stores during the COVID-19 induced shutdown, a market release on 25 May 2020 announced the staged reopening of stores within the ANZ segment and positive news of cost efficiencies achieved during the lockdown such as navigating working capital efficiencies, deferring non-essential capex spending, negotiated rental reductions and JobKeeper Subsidy Scheme eligibility for employees. City Chic's achieved 57% online sales growth during the shutdown period in comparison to the same period last year and as customers shifted focus in styles, City Chic repositioned its product and stock mix to better suit these demands. This flexibility signifies the strength of the online retailer model for CCX as well as the strong capital position of the business. The update saw the share price up 3.5% by the end of the week following the release.

CCX was introduced to the fund on 18 May 2020 and we remain confident in its return potential. Zion Capital view this niche offering as an opportunity in the consumer discretionary sector with both demographic and structural tailwinds supporting its growth.

IPH Ltd (ASX:IPH)

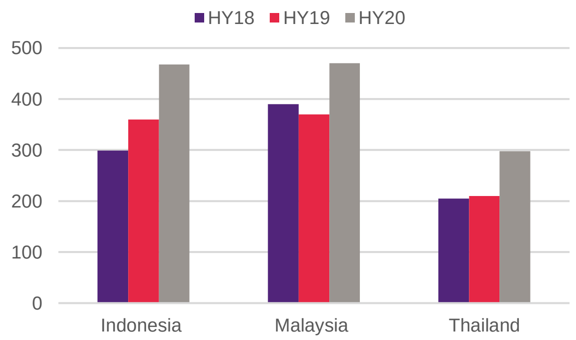
IPH Limited (IPH) is a holding company for numerous subsidiaries operating within the intellectual property management services industry across the regions of Australia, New Zealand, Singapore, and South-East Asia.

Experiencing strong growth in the past few years with a 3-year revenue and EBITDA CAGR of 21.9% and 15.6% respectively, IPH is a fundamentally sound business in a structurally growing industry. Maintaining sizeable market share within the Australian & NZ (36.9%), Singapore (22.3%) and growing Asian patent markets, the company maintains strong margins (30.6% EBITDA HY20) and combined with the scale of the company's operations this provides them with an undisputedly strong economic moat. Furthermore, IPH's business model is quite resilient to the effects of COVID-19 due to the long-dated nature of patent work and the day-to-day nature of electronic fillings and communications. This resilience if further reinforced by the company's strong balance sheet position with cash and net debt of $62m and $104m respectively as at 20 April.

IPH has a strong track record of successfully integrating acquisitions across core and secondary markets to enhance organic growth opportunities. The company recently reported a strong HY20 performance with double digit growth in its Asian IP segment and $1.3m in captured cost synergies regarding its recent acquisition of Xenith IP, previously one of the company's main Australian competitors. Overall, we believe as management continues to identify acquisition opportunities to grow IPH's share in developing Asian markets and their dominant position in core markets is further solidified through margin expansion and additional service offerings, IPH's growth potential exceeds its current 19.69x forward earnings multiple as at May 31 2020.

Additionally, the Zion team was presented with the opportunity to meet with IPH management in the form of the company's CEO and Managing Director, Dr Andrew Blattman. It was insightful to get a clear picture of the vision Andrew has for IPH moving forward and the passion he has for the company. Overall, the comprehensive experience and aligned objectives of the broader management team, gives Zion conviction that moving forward, management will continue to create value enhancing opportunities for shareholders.

The following figure depicts the total patent cases lodged in the largest 3 Asian jurisdictions, Indonesia, Malaysia, and Thailand which grew 30%, 26.5%, and 42.3% in HY20, respectively.



Source: Company Reporting Internal Filing Statistics

Portfolio Management Team

Name	*Current Enrolment and Contact*
Golden Chen	Bachelor of Advanced Finance & Economics golden.chen@uq.net.au
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Quantitative Data:

SMIF Portfolio Holdings:

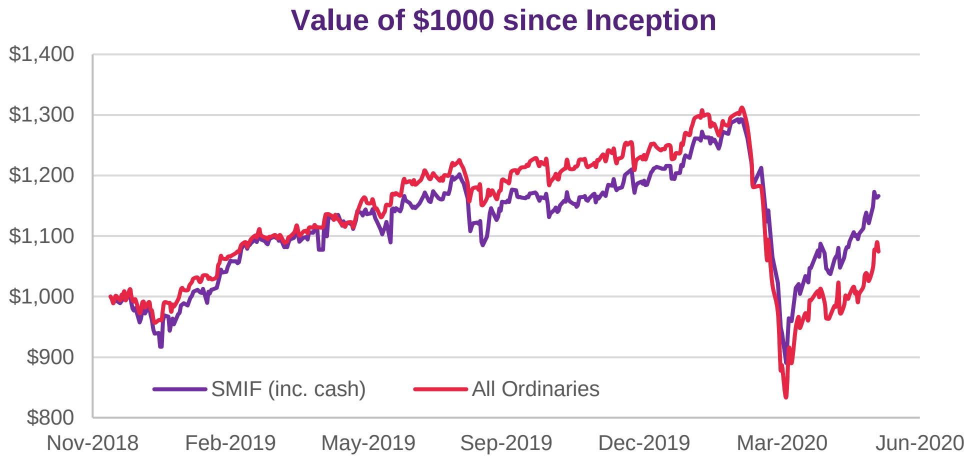
Ticker	Company Name	Portfolio Weight	Position 29th May	Return*
CNU	Chorus Limited	6.2%	$14,293	27.3%
MQG	Macquarie Group Limited	5.9%	$13,636	-13.4%
BRG	Breville Group Limited	5.8%	$13,483	23.6%
RMD	ResMed Inc.	5.8%	$13,402	16.5%
NST	Northern Star Resources Limited	5.1%	$11,944	42.2%
APA	APA Group	4.5%	$10,519	2.4%
APX	Appen Limited	4.0%	$9,271	75.8%
BHP	BHP Group	3.9%	$9,145	8.0%
CSL	CSL Limited	3.9%	$9,115	22.5%
RIO	Rio Tinto Group	3.6%	$8,499	3.9%
MICH	Magellan Infrastructure Fund	3.6%	$8,395	-11.6%
SHL	Sonic Healthcare Limited	3.5%	$8,085	28.4%
JHX	James Hardie Industries plc	3.4%	$7,993	-0.1%
WOW	Woolworths Group Limited	3.1%	$7,209	-5.6%
PWH	PWR Holdings Limited	3.1%	$7,152	14.7%
QUB	Qube Holdings Limited	2.9%	$6,816	5.2%
INA	Ingenia Communities Group	2.8%	$6,584	16.3%
SCP	Shopping Centres Australasia Property Group	2.7%	$6,306	-14.5%
SYD	Sydney Airport Limited	2.7%	$6,254	-31.6%
CCX	City Chic Collective Limited	2.6%	$6,030	22.9%
SSM	Service Stream Limited	2.4%	$5,524	-4.1%
IPH	IPH Limited	2.3%	$5,277	1.1%
IDX	Integral Diagnostics Limited	2.3%	$5,232	9.3%
COE	Cooper Energy Limited	2.1%	$4,918	0.7%
WBC	Westpac Banking Corporation	2.1%	$4,822	-38.1%
JLG	Johns Lyng Group Limited	2.0%	$4,586	2.5%
BAP	Bapcor Limited	1.8%	$4,099	-18.3%
	Cash and Dividends Receivable	5.9%	$13,592	
		TOTAL	**$232,181**	

*Total return on each position since purchase, net of fees, excluding dividends

Performance:

	1 month	3 months	6 months	12 months	Inception (Nov 2018)*
SMIF	7.9%	-1.4%	-3.2%	3.7%	16.1%
All Ordinaries Accumulation Index	5.0%	-9.0%	-14.1%	-6.2%	7.4%
Alpha	2.9%	7.6%	11.0%	9.9%	8.7%

*Total return since fund inception on 19 November 2018 based on initial $200,000 investment.



Key Portfolio Metrics (medians):

Metric	
Trailing P/E	28.9x
P/B	3.9x
ROE	16.5%

Market Capitalisation Breakdown:

	Number of Stocks	% Weight
ASX1-100	13	53.0%
ASX101-200	9	27.7%
ASX201-300	0	0.0%
ASX301-500	5	13.5 %
Cash and Dividends Receivable		5.9%

Sector Breakdown:

	% Weight	Change in rank
Materials	17.2%	-
Healthcare	16.4%	-
Consumer Discretionary	14.1%	▲3
Industrials	13.0%	▲3
Financials	12.3%	▼1
Communication Services	6.5%	▼3
Real Estate	5.9%	▲3
Utilities	4.8%	▲1
Information Technology	4.2%	▼1
Consumer Staples	3.3%	▼4
Energy	2.2%	-

Information on the Fund and Disclaimer

This update has been prepared by the student portfolio managers of the University of Queensland Business School Student Managed Investment Fund. The Fund was seeded by the University with $200,000 in 2018 and the first investments were made in November 2018. The University of Queensland is the sole owner of the assets in the Fund and no fees are payable by the University for the management of the Fund. The Fund recognises the support of Morgans Brisbane as stockbroker to the Fund.

The information in this update is prepared primarily for educational purposes and to keep internal and external Fund stakeholders informed. Any views expressed in this update are the views of the student portfolio managers. The accuracy, reliability or completeness of data or information presented in this update is not guaranteed. The information is not intended as a securities recommendation or statement of opinion intended to influence a person or persons in making a decision in relation to an investment.