Lonsec

5 Highly Recommended

Product Review
Smallco Broadcap Fund

ISSUE DATE 25-09-2023

About this Review

ASSET CLASS REVIEWED	AUSTRALIAN EQUITIES
SECTOR REVIEWED	AUSTRALIAN LARGE CAP
SUB SECTOR REVIEWED	GROWTH
TOTAL FUNDS RATED	24

About this Fund

ASIC RG240 CLASSIFIED	NO
FUND REVIEWED	SMALLCO BROADCAP FUND
APIR CODE	ASC0003AU
PDS OBJECTIVE	TO OUTPERFORM THE BENCHMARK BY 5% P.A., AFTER FEES, ON A ROLLING THREE-YEAR BASIS
INTERNAL OBJECTIVE	SAME AS THE PDS OBJECTIVE
STATED RISK OBJECTIVE	INFORMATION RATIO GREATER THAN ONE OVER ROLLING THREE-YEAR PERIODS
DISTRIBUTION FREQUENCY	ANNUALLY
FUND SIZE	$251.9M (JULY 2023)
FUND INCEPTION	31-07-2008
ANNUAL FEES AND COSTS (PDS)	1.78% P.A. (INCL. PF COST ESTIMATE 0.46%)
PERFORMANCE FEE	15% (OF ANY OUTPERFORMANCE ABOVE THE BENCHMARK)
RESPONSIBLE ENTITY	SMALLCO INVESTMENT MANAGER LIMITED

About the Fund Manager

FUND MANAGER	SMALLCO INVESTMENT MANAGER LIMITED
OWNERSHIP	100% STAFF OWNED
ASSETS MANAGED IN THIS SECTOR	$766.8M (JULY 2023)
YEARS MANAGING THIS ASSET CLASS	23

Investment Team

PORTFOLIO MANAGER	ANDREW HOKIN
INVESTMENT TEAM SIZE	7
INVESTMENT TEAM TURNOVER	LOW
STRUCTURE / LOCATION	CENTRALISED / SYDNEY

Investment process

STYLE	GARP
TYPICAL CAPITALISATION BIAS	ALL-CAP
BENCHMARK	S&P/ASX 300 ACCUMULATION INDEX
TYPICAL NUMBER OF STOCKS	20 -30
STOCK LIMITS	MAXIMUM 15% AT COST / 20% AT CURRENT VALUATION
SECTOR LIMITS	MAXIMUM 20% (SOFT)
CASH LIMIT	50%

Fund rating history

SEPTEMBER 2023	HIGHLY RECOMMENDED
SEPTEMBER 2022	HIGHLY RECOMMENDED
SEPTEMBER 2021	HIGHLY RECOMMENDED

What this Rating means

The **'Highly Recommended'** rating indicates that Lonsec has very strong conviction the financial product can generate risk adjusted returns in line with relevant objectives. The financial product is considered a preferred entry point to this asset class or strategy.

Strengths

- Boutique investment culture, supported by strong alignment with high equity ownership among key investment personnel.
- Quality investment team led by well-regarded Portfolio Manager, Andrew Hokin, who possesses considerable experience in small and mid-cap investing.
- The Manager has displayed a disciplined approach to capacity management, having previously closed the Fund to investors when the capacity limit was reached.
- The Fund has a strong track record of outperformance since inception.

Weaknesses

- The total fee load of the Fund is expensive relative to peers.
- While noting the Fund's outperformance since inception, the persistently elevated cash holding has been a drag on performance.

Fund Risk Characteristics

	LOW		MODERATE		HIGH
BUSINESS SUSTAINABILITY RISK				●	
CAPITAL VOLATILITY					●
SECURITY CONCENTRATION RISK				●	
SECURITY LIQUIDITY RISK			●		

Risk categories are based on Lonsec's qualitative opinion of the risks inherent in the financial product's asset class and the risks relative to other financial products in the relevant Lonsec sector universe.

BIOmetrics

Aggregated risks

	1	2	3	4	5	6	7
STD RISK MEASURE						●	

A Standard Risk Measure score of 6 equates to a Risk Label of 'High' and an estimated number of negative annual returns over any 20 year period of 4 to less than 6. This is a measure of expected frequency (not magnitude) of capital losses, calculated in accordance with ASFA/FSC guidelines.

	LOW	MODERATE	HIGH
RISK TO INCOME		●	

ANALYST: MITCHELL RYAN | APPROVED BY: RICHARD DALIDOWICZ

Smallco Broadcap Fund

Features and benefits

	LOW		MODERATE		HIGH
COMPLEXITY		●			
ESG	●				

Fee profile

	LOW	MODERATE	HIGH
FEES VS. UNIVERSE			●
FEES VS. ASSET CLASS			●
FEES VS. SUB-SECTOR			●

Fee BIOmetrics are a function of expected total fee as a percentage of expected total return.

What is this Fund?

- The Smallco Broadcap Fund ('the Fund') is a concentrated, 'benchmark-unaware' Australian equity product. The Fund adopts an all-cap approach seeking to invest in companies that are likely to exceed consensus earnings expectations or stocks that are out of favour and are expected to at least meet earnings expectations. The Fund aims to outperform the S&P/ASX 300 Accumulation Index ('the Benchmark') by 5% p.a., before fees, over rolling three-year periods.
- Smallco Investment Manager Limited (the 'Manager') believes it can source investment opportunities with above-average return potential by conducting rigorous fundamental analysis into a company's earnings and cash generation abilities, management quality, and industry characteristics. The Manager prefers to use bottom-up analysis as opposed to top-down, macroeconomic research to identify investment opportunities.
- Despite the all-cap approach, the Manager has a focus on smaller market capitalisation companies, believing there are greater inefficiencies within this segment of the market. The Fund has typically held between 25-40% of the portfolio in companies with a market capitalisation of less than $1bn.
- The Fund generally avoids stocks with more cyclical earnings such as retail, building materials and resources. However, there may be occasions where it will make investments in cyclical stocks based on a top-down view. It also avoids companies with embryonic business models e.g. biotechnology, believing that earnings are too difficult to forecast.
- The Fund adopts a concentrated, 'benchmark unaware' approach, holding between 20-30 stocks. The Fund is governed by relatively flexible risk constraints, with individual sector and stock weights permitted to reach 20% of the total portfolio. Furthermore, the Fund can hold up to 50% of the portfolio in cash, noting this allocation is primarily driven by the unavailability of attractive investment opportunities i.e. limited opportunities would warrant a higher cash weight.
- The Fund's PDS dated 31 March 2023 disclosed Annual Fees and Costs ('AFC') totalling 1.78% p.a. This comprises (1) Management Fees and Costs of 1.2% p.a., (2) Performance Fees of 0.46% p.a., and (3) Net Transaction Costs of 0.12% p.a. In line with RG97, some fees and costs have been estimated by the issuer on a reasonable basis. Actual fees and costs may vary from these estimates, particularly with respect to net transaction costs.
- The performance fee is charged at 15% of the excess return above the S&P/ASX 300 Accumulation Index. The performance fee is subject to a 'high watermark' requirement and only payable where the exit price at the end of the calculation period exceeds the high watermark. The high watermark does not have a reset period.
- The Fund charges buy/sell spreads set at 0.45%/0.45%. These spreads can be subject to change, most notably during periods of market volatility, and can be sourced from the Manager's website during such times.
- Lonsec also has research coverage of the Smallco Investment Fund (APIR code: ASC0001AU), which is managed utilising a consistent investment process to the Fund. However, it also has the ability to short and gear, and therefore, charges a higher management cost and performance fee.

Using this Fund

This is General Advice only and should be read in conjunction with the Disclaimer, Disclosure and Warning on the final page.

- Lonsec notes that the Manager has produced a Target Market Determination (TMD), which forms part of the Responsible Entity's Design and Distribution Obligations for the Fund. Lonsec has collected the TMD that has been provided by the Manager and notes that this should be referred to for further details on the Target Market Summary, Description of Target Market and Review Triggers.
- The Fund is a long-only Australian equity product, which will be invested in the Australian equity market. Investors should be aware that returns may vary materially from traditional equities indices and other more benchmark aware Australian equity products. Lonsec considers it suitable for blending with other Australian equity strategies including style biased, long/short and absolute return products. Lonsec recommends that equity investments are suitable for investors with an investment time horizon of at least five years.
- The Fund is subject to equity market risks, and movements (both positive and negative) in the prices of the underlying securities will impact the portfolio. Investors should therefore be aware of and comfortable with the potential for the Fund to experience periods of negative returns, which result in capital losses being incurred on their investment. As such, the Fund will generally sit within the growth component of a diversified investment portfolio.

Suggested Lonsec risk profile suitability

SECURE	DEFENSIVE	CONSERVATIVE	BALANCED	GROWTH	HIGH GROWTH
		●	●	●	●

For guidance on appropriate asset allocations and risk profiles, refer to the latest Lonsec Strategic Asset Allocation Review and Risk Profile Definitions on our website.

Changes Since Previous Lonsec Review

- There have been no material changes to the investment process or team since Lonsec's previous review.

Smallco Broadcap Fund

Lonsec Opinion of this Fund

People and resources

- The investment team comprises seven investment professionals, of which three of the most senior members had previously worked alongside each other at ANZ Securities. While the team tends to adopt a collective decision-making philosophy, Andrew Hokin is named portfolio manager of the Fund and ultimately accountable for its performance.
- Lonsec observed Hokin to have made a strong contribution to bringing appropriate technical knowledge on both the market and stocks to his portfolio management duties. In Lonsec's view, Hokin has also been instrumental in strengthening the rigour of the Manager's investment process, particularly through the introduction of the improved Quality Rating System assessment. Hokin appears highly motivated and is viewed as a key attraction of the Fund.
- Hokin sits alongside the six remaining members of the investment team, namely Rob Hopkins, Bill Ryan, Craig Miller, Paul Graham, Adam Simpson and Han Xu. The investment team exhibits notable co-tenure working together at the Manager and/or at other investment management firms. Pleasingly, there have been no departures from the investment team since the inception of the firm in 2000.
- Lonsec has observed a highly performance-driven culture at the firm, one which to date has proven to be conducive to a stable environment with a clear alignment of interests between the investment team and end investors. Hopkins and Ryan remain large equity owners and pleasingly, equity has been afforded to other investment team members, serving to strengthen their engagement with the firm. Additionally, there is a high level of co-investment among staff and the performance fee structure further aligns their interests.
- Key person risk is considered to be high in Hokin, and extends to co-founders Hopkins and Ryan given their integral involvement in the Manager's investment process and broader business. Lonsec acknowledges the equity ownership structure to be a significant mitigating factor, while also noting Hokin's tenure at the firm. Further, the involvement of Simpson from a succession planning perspective also tempers this risk somewhat, noting he serves as the lead portfolio manager for the Smallco Investment Fund. Nonetheless, Lonsec would view the departure of these individuals to be a material event.

Research and portfolio construction

- The Manager's investment philosophy is centred on identifying companies that are likely to exceed consensus earnings estimates in the medium term given pricing inefficiencies are likely to be more prevalent in smaller market capitalisation names. This leads the Manager to seek out a core group of undervalued quality companies through criteria that favours companies with a high cash generation ability, attractive earnings outlooks and strong competitive advantages. This is supplemented by opportunistic value ideas where a six to 12-month re-rating trigger exists. Lonsec believes the Manager has demonstrated an investment edge in companies with a market capitalisation between $100-500m.
- The investment process is considered to be pragmatic and bespoke to the Manager's philosophy through a focus on understanding the key drivers of earnings. Engagement with company management features prominently and underpins the internal research effort, with two investment team members attending each meeting. Lonsec highlights the strong emphasis placed on meeting with company management, believing this to be conducive to high-conviction, concentrated approaches. Lonsec has reviewed the Manager for a number of years and has developed strong conviction in the Manager's bottom-up research process.
- The Manager also leverages sell-side research in the preliminary stages of the investment process, primarily to expedite the process of familiarisation with new companies and industries. Lonsec notes, however, that internally generated research is the driver of investment decisions. Valuation is based on a range of multiples-based tools that are forecasted over a three-year investment horizon. The Manager's dual coverage approach to stocks extends to financial modelling and is considered to promote robustness in challenging key inputs into the models and assist in proving/disproving investment theses. Lonsec considers the approach to be positive and encourages procedural rigour to the investment process.
- Portfolio construction is consultative but ultimately led by Hokin who is responsible for constructing a portfolio reflecting the Manager's highest conviction ideas. Portfolio construction is primarily driven by the Manager's Quality Rating System to aid in limiting exposure to lower-quality names that are trading at attractive prices. Lonsec considers the portfolio construction process to be robust, with a clear link between the team's conviction in each stock, the assessment of its risk and its weight within the portfolio.
- The Fund can exhibit a high degree of concentration at individual stock and sector levels, with up to 15% of the portfolio invested in a single stock. While this limit is infrequently fully utilised, Lonsec has observed instances where the Fund has been more aggressive in building up positions relative to peers.
- Positions are trimmed as they approach the Manager's assessment of their intrinsic value, and are typically sold when they surpass their predicted valuation or there is a negative change in the company's fundamentals. However, Lonsec notes the flexibility around sell discipline with the Manager previously exhibiting a tendency to

tolerate holding 'growth' stocks with high valuations if their fundamental growth story remains intact. Notwithstanding, Lonsec considers the Manager to be more pragmatic in reducing positions as they approach the investment team's predicted valuation relative to some of its peers, and is more active in selling positions judged to be lower quality and/or with more cyclical earnings.

- The Fund's ability to hold up to 50% in cash adds a defensive tilt to the portfolio and is utilised when investment opportunities are not readily available. The Fund's cash balance has averaged around 13.8% since Lonsec's previous review, and the Manager has demonstrated in the past its ability to utilise the extent of its cash limit. Nonetheless, Lonsec notes that the persistently high cash weight has been a drag on performance since inception and, although Lonsec has been encouraged by the Manager's disciplined approach to capacity management, may be an indication of capacity/liquidity concerns.

ESG integration

- Lonsec's ESG integration assessment considers how rigorous, robust and structured the ESG process for the Fund is as well as how well it integrates into the overall investment process and the Manager's overall policy and reporting framework. The assessment is not intended to assess the underlying holdings of the Fund's portfolio or the Manager's adherence to any form of impact, green / sustainable or ethical standards.
- At the overall corporate level Lonsec views the Manager's overall ESG framework as significantly behind peers. The Manager has not articulated a commitment to integrating ESG within their investment process to Lonsec. There is no evidence in their public positioning, nor does the Manager seem to have any ESG-related policies or frameworks in place.
- The Manager has indicated that their Responsible Investment style is "ESG Integration" and as such they take Environmental, Social and Governance factors into consideration when assessing investment opportunities. With a primary ESG style of "Stewardship" Managers will usually focus their ESG strategy on Engagement and Voting as the key tool in managing their ESG risks. While stewardship approaches are common across most Managers, they can form the key ESG strategy employed by some managers. Due to the qualitative nature of this style, Lonsec highlights the need for managers to provide clear and detailed reporting on both engagement and voting activities and recommends investors review the fund stewardship reporting where available.
- Within the management of this specific Fund, Lonsec notes:
  - The Manager has no observable structured approach to the collection of ESG data within their investment process. The Manager does not source general external ESG data instead relying on collecting its own ESG data through company meetings and websites. Lonsec believes that this is less robust than peers.
  - There is no focused internal ESG research carried out by the Manager for this Fund.
  - There is no relationship between ESG factors and the stock selection process.
  - While some ESG rules drive exclusions or position caps, there is no clear use of portfolio-level measurement of ESG characteristics apparent. There are no portfolio-level ESG-based limits or targets in place for the Fund.
  - While the Manager has systems in place to track engagements, evidence of actual engagement to deliver ESG objectives is minimal. There is no clear system for prioritising engagements or for measuring success.
  - ESG does not form a component of the Manager's broader compliance framework and overall transparency provided to investors is lagging. Pleasingly voting on the Fund is directed by the Fund's portfolio manager directly.

Risk management

- Lonsec believes the Manager has adequate risk controls in place to manage the portfolio, although notes that risk management is largely embedded within the Manager's bottom-up investment process.
- The Fund's design means there are minimal formal portfolio risk limits, albeit Lonsec highlights that this is in line with other high-conviction peers. The potential stock concentration in the Fund is high with a single stock being up to 20%, at current valuation, of the portfolio. Furthermore, exposure to any one sector can be significant, although closely monitored by the Manager. Portfolio risk limits comprise at least four GICS sectors with a maximum of 20%.
- The Manager's Quality Rating System assigns a score to each stock in the portfolio from which a weighted average quality rating is calculated for the Fund. An internal portfolio construction rule requires the Fund to meet a minimum quality score. Lonsec believes the use of these scores assists the Manager in avoiding unintended risk within the portfolio, enhances sell discipline, and ensures exposure to lower quality and cyclical stocks are controlled.
- The Fund also employs a separate 25% limit on total exposure to what is assessed as lower-quality companies. The Manager has a relatively broad definition of what constitutes lower quality, which includes most non-major resource and mining service stocks, and companies that are considered to be in structurally impaired industries. Additionally, the Fund can invest up to 30% of the portfolio in stocks that are deemed to be illiquid. While Lonsec considers the allocation to be generous, these are consistent with the Manager's tight capacity management.

Capacity management

- Firmwide FUM as of 31 July 2023 was approximately $766.8m, including $251.9m in the Fund. In April 2020, the Manager reopened both the Fund and the Smallco Broadcap Fund to new and existing investors.
- Historically, Lonsec has observed prudent discipline by the Manager in relation to capacity management, having previously closed the Fund to investors when capacity was reached. Pleasingly, the Manager has continued to demonstrate prudent judgement through the Fund's reopening. Lonsec is supportive

of the Manager's discipline, which should help preserve the Fund's appeal.

Fees

- Lonsec considers the AFC of the Fund (1.78% p.a.) to be excessive relative to peers and the broader Australian equity peer group.
- Lonsec is generally supportive of performance fees so long as they are appropriately structured. In this case, Lonsec notes that to qualify for a performance fee the Fund must outperform its Benchmark, which is reasonable, albeit, misaligned with the Fund's investment objective. In addition, the fee is subject to a high watermark. Overall, the performance fee structure is considered suitable, albeit a hurdle rate in line with the Fund's investment objective would be viewed positively by Lonsec.
- The buy/sell spread is 0.45%/0.45% and net transaction costs disclosed under RG97 reporting regime are 0.12% p.a., thus Lonsec considers the buy/sell spreads to have been operating ineffectively and this will remain a watchpoint in future reviews.

Product

- The Fund is a relatively vanilla-listed Australian equity strategy. Hence, Lonsec does not consider it to be operationally challenging to implement. Smallco Investment Manager Limited is the Responsible Entity ('RE') of the Fund and thus is a related entity. The RE is responsible for operating and managing the MIS, holds an AFSL and as such is required to comply with its AFSL and RE obligations as outlined under the Corporations Act. Lonsec notes the RE has built experience in operating and managing over an extended period and is expected to have a governance framework in place to deal with any perceived conflicts of interest.

Performance

- The Fund aims to outperform the S&P/ASX 300 Accumulation Index ('the Benchmark') by 5% p.a., before fees, over rolling three-year periods. All performance figures noted below are as at 31 July 2023 and net of fees.
- Over the three-year period, the Fund generated a return of 16.7% p.a., comfortably outperforming the Benchmark and peers by 4.8% p.a. and 7% p.a., respectively, albeit noting the Fund slightly missed its investment objective. Over the five-year period, the Fund returned 9.2% p.a. to outperform the Benchmark by 1.7% p.a. Furthermore, the Fund's performance has been notable since inception, generating an outperformance of 8.7% p.a.
- The Fund delivered solid performance over the 12 months of 13.9% to outperform the Benchmark and peers by 2.8% and 3.2%, respectively.
- Lonsec notes the Fund has displayed elevated volatility relative to both peers and the Benchmark across all time periods, albeit noting this outcome is largely expected given the concentrated approach and the persistent small- to mid-cap bias observed. That said, the Fund has not achieved its risk objective of maintaining and Information Ratio greater than 1 over rolling-three year periods, with a ratio of 0.51 over this period.

Overall

- Lonsec has maintained the Fund's **'Highly Recommended'** rating at its most recent review. Supporting the rating is Lonsec's strong conviction in the capability and investment skill of Portfolio Manager Andrew Hokin, who is supported by a high quality investment team with notable co-tenure. Furthermore, the Manager has continued to demonstrate prudent discipline in relation to capacity management, which serves to preserve the Fund's investment appeal.
- Detracting from the rating is the Fund's total fee load, which is expensive relative to peers. Additionally, Lonsec is wary of high allocations to illiquid holdings and cash.

People and Resources

Corporate overview

Smallco Investment Manager Limited is a boutique funds management firm based in Sydney. The firm was founded in April 2000 by Rob Hopkins and Bill Ryan and remains privately owned by senior members of the investment team. The firm specialises in managing small and mid-cap Australian Equity strategies, with $766.8m of funds under management ('FUM') as of July 2023 across three strategies.

Size and experience

NAME	POSITION	EXPERIENCE INDUSTRY / FIRM
ROB HOPKINS	MANAGING DIRECTOR	37 / 23
BILL RYAN	PORTFOLIO MANAGER	27 / 23
CRAIG MILLER	PORTFOLIO MANAGER	18 / 18
ANDREW HOKIN	PORTFOLIO MANAGER	28 / 16
PAUL GRAHAM	PORTFOLIO MANAGER	28 / 9
ADAM SIMPSON	PORTFOLIO MANAGER	20 / 6
HAN XU	PORTFOLIO MANAGER	16 / 5

The investment team comprises seven investment professionals with an average 25 years of investment experience. The team is led by Managing Director Rob Hopkins and Executive Director Bill Ryan.

Hopkins with 37 years of industry experience has previously led small companies research at brokerage firms Macquarie Equities, BT Alex Brown, ANZ Securities and Macintosh Securities. Ryan with 27 years of industry experience previously worked at ANZ Securities.

Hokin with 28 years of industry experience has been with the Manager since July 2007 and previously worked at brokerage firms Day Cutten and Macquarie Securities.

Team structure

The Fund is managed by Hokin, while Hopkins manages the Smallco Investment Fund. Craig Miller, Paul Graham, Adam Simpson and Han Xu are responsible for research and providing support to the portfolio managers. Miller also serves as the firm's day-to-day business manager.

Remuneration / Alignment of interests

All key investment professionals have either equity ownership or profit share arrangements. Additionally, there is a high level of co-investment among staff.

Smallco Broadcap Fund

Research Approach

Overview

RESEARCH PHILOSOPHY	FUNDAMENTAL, BOTTOM-UP
TARGET COMPANY	COMPANIES WHICH ARE LIKELY TO EXCEED CONSENSUS EARNINGS EXPECTATIONS OR OUT OF FAVOUR
MINIMUM MARKET CAPITALISATION	$100M (SOFT)
NUMBER OF STOCKS IN MANAGER'S UNIVERSE	500
NUMBER OF STOCKS FULLY MODELLED/RESEARCHED	115
RESEARCH INPUTS	COMPANY MEETINGS (MANAGEMENT, COMPETITORS, SUPPLIERS), INDUSTRY ANALYSIS
BROKER RESEARCH	MINOR CONSIDERATION
VALUATION OVERVIEW	PRICE-TO-EARNINGS RATIO, EBIT/EBITDA AND PRICE-TO-CASHFLOW MULTIPLES

Universe filtering

The investment universe is initially screened for a minimum market capitalisation of $100m. The Manager then applies a Porter-style Quality Rating System filter with each stock reviewed and assigns a numerical rating, between 0 to 10, based on its quality and cyclicality. The refined investment universe comprises approximately 115 stocks, which are considered candidates for further bottom-up, fundamental research.

The Manager will typically underweight resource stocks, biotechnology companies and companies with cyclical earnings.

Research approach

Meetings with company management form part of the bottom-up research process with the aim of identifying companies likely to exceed consensus earnings estimates. Company meetings provide a forum to prove/disprove the investment thesis with two members of the investment team assigned to each stock in the refined universe.

Top-down and macroeconomic analysis does not feature heavily in the investment process, and is rather used as a feedback mechanism to assist in concentrating the Manager's bottom-up research effort.

Valuation

The valuation process is comprised of an amalgamation of multiples-based accounting ratios such as Price-to Earnings ratio, and EBIT/EBITDA and Price-to-Cashflow multiples. Multiple accounting ratios are implemented to compare a company's current trading price against the Manager's assessment of its intrinsic value.

Portfolio Construction

Overview

FUND BENCHMARK	S&P/ASX 300 ACCUMULATION INDEX
INTERNAL RETURN OBJECTIVE	TO OUTPERFORM THE BENCHMARK BY 5% P.A., AFTER FEES, OVER ROLLING THREE-YEAR PERIODS
INTERNAL RISK OBJECTIVE	INFORMATION RATIO GREATER THAN ONE OVER ROLLING THREE-YEAR PERIODS
PORTFOLIO MANAGEMENT APPROACH	BENCHMARK UNAWARE, CONCENTRATED
INVESTMENT STYLE	GARP
PORTFOLIO DECISION MAKING	PORTFOLIO MANAGER CONSENSUS
STOCK SELECTION	BOTTOM-UP
TOP-DOWN INFLUENCE	MINOR CONSIDERATION
MARKET CAPITALISATION BIAS	ALL-CAP
TYPICAL NUMBER OF HOLDINGS	20 – 30
EXPECTED PORTFOLIO TURNOVER	20% P.A.
OBSERVED ACTIVE SHARE	95.8% (JULY 2023)
PORTFOLIO EXPOSURE IN TOP 10 HOLDINGS	52.9% (JULY 2023)

Decision making

Portfolio construction is the responsibility of Hokin. However, given the collective decision-making philosophy, consensus views will also have some influence on positioning. The Manager aims to construct a portfolio with 20-30 of the most attractive stocks, primarily based on the current discount to valuation, as identified during the research phase while taking into account the portfolio risk limits.

Position sizing is primarily at the discretion of Hokin, with sizing dependent on a company's discount to its intrinsic value and score from the proprietary Quality Rating System. Additional factors considered in position sizing include the Fund and stocks' liquidity, risk of sustained capital loss, and likely investment outcomes. In general, positions of 3%, 5% or 7% will be implemented, with the ability of a position to extend up to 15% (at cost) and 20% (at current valuation).

Buy and sell drivers

At a high level, stocks that trade below the Manager's assessment of their intrinsic value, combined with sound company management, high cash generation ability, strong competitive position and attractive earnings outlook are candidates for portfolio inclusion. Conversely, stocks are sold when they reach the Manager's predicted valuation or if there is a negative change in the company's fundamentals.

Risk Management

Risk limits

SEPARATE INVESTMENT RISK MONITORING	NO
STOCK LIMITS	MAXIMUM 15% AT COST / 20% AT CURRENT VALUATION
SECTOR / INDUSTRY LIMITS	EXPOSURE TO AT LEAST FOUR GICS SECTORS
CASH LIMIT	MAXIMUM 50%
USE OF DERIVATIVES	NOT PERMITTED

The Fund is managed with a broad range of risk limits at the stock and sector level in absolute terms. Position sizes are limited to 15% of the portfolio at cost, to a maximum of 20% at current valuation. Sector exposures comprise at least four GICS sectors with a maximum of 20% (soft).

Smallco Broadcap Fund

Other limits implemented include restricting the exposure to securities deemed illiquid to a maximum 30% of the portfolio and limiting exposure to companies with a market capitalisation below $1bn to 40% of the portfolio.

Risk monitoring

The Manager monitors a range of performance metrics, including quarterly attribution relative to the Benchmark. Diversification, risk, quality, cyclicality and liquidity controls in place are monitored daily.

Fund performance and positions with respect to its risk parameters are formally considered at the quarterly board meeting where, in particular, diversification at the stock and sector level, and liquidity are considered.

Risks

An investment in the Fund carries a number of standard investment risks associated with investment markets. These include performance, liquidity, counterparty, market and tax risks. These and other risks are outlined in the PDS and should be read in full and understood by potential investors. Lonsec considers the following to be the major risks:

Equity market risk

Investments in equity markets are subject to numerous factors which may have an impact on the performance of an investment, both positive and negative. Unexpected changes in economic, technological, structural, regulatory or political conditions can have an impact on the returns of all investments within a particular market.

Liquidity risk

The Fund may encounter difficulties or be unable to sell some of its asset due to factors specific to that investment or prevailing market conditions. It may also potentially result in delays in processing, or even the suspension of redemptions if some of its assets are unable to be sold.

Smallco Broadcap Fund

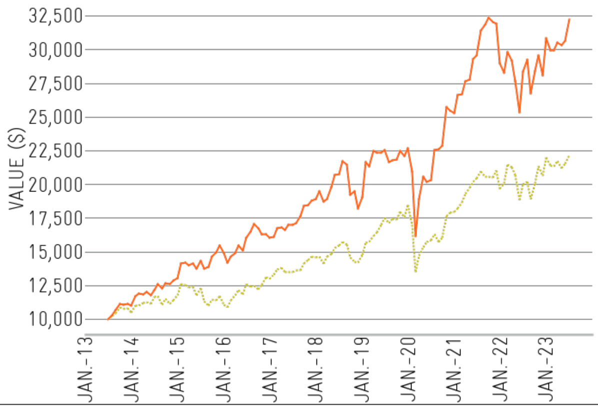
Quantitative Performance Analysis - annualised after-fee % returns (at 31-7-2023)

Performance metrics

	1 YR		3 YR		5 YR		10 YR	
	FUND	PEER MEDIAN	FUND	PEER MEDIAN	FUND	PEER MEDIAN	FUND	PEER MEDIAN
PERFORMANCE (% PA)	13.88	10.64	16.72	9.75	9.18	7.43	12.43	9.49
STANDARD DEVIATION (% PA)	17.47	14.67	18.30	15.17	22.05	16.53	17.00	13.84
EXCESS RETURN (% PA)	2.79	-1.74	4.81	-2.06	1.73	-0.28	4.13	0.96
OUTPERFORMANCE RATIO (% PA)	58.33	41.67	47.22	47.22	46.67	49.17	55.83	54.17
WORST DRAWDOWN (%)	-8.46	-6.73	-21.59	-20.19	-28.63	-25.21	-28.63	-25.44
TIME TO RECOVERY (MTHS)	2	4	NR	NR	7	10	7	12
SHARPE RATIO	0.61	0.52	0.85	0.62	0.36	0.37	0.63	0.54
INFORMATION RATIO	0.43	-0.43	0.51	-0.41	0.16	-0.06	0.47	0.22
TRACKING ERROR (% PA)	6.51	4.65	9.52	5.92	10.62	5.76	8.88	5.41

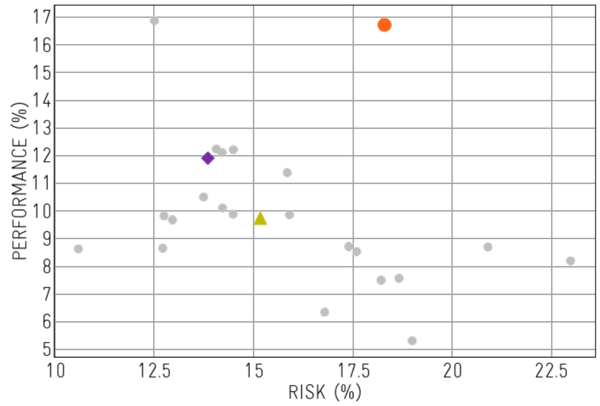
PRODUCT: SMALLCO BROADCAP FUND
LONSEC PEER GROUP: AUSTRALIAN EQUITIES - AUSTRALIAN LARGE CAP - GROWTH
PRODUCT BENCHMARK: S&P/ASX 300 TR INDEX AUD
CASH BENCHMARK: BLOOMBERG AUSBOND BANK BILL INDEX AUD
TIME TO RECOVERY: NR - NOT RECOVERED, DASH - NO DRAWDOWN DURING PERIOD

Growth of $10,000 over 10 years



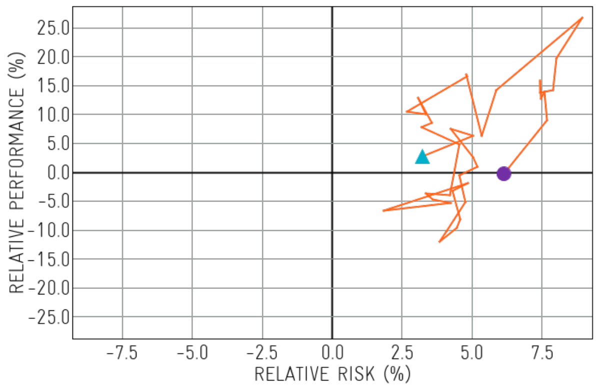
SMALLCO BROADCAP FUND
S&P/ASX 300 TR INDEX AUD

Risk-return chart over three years



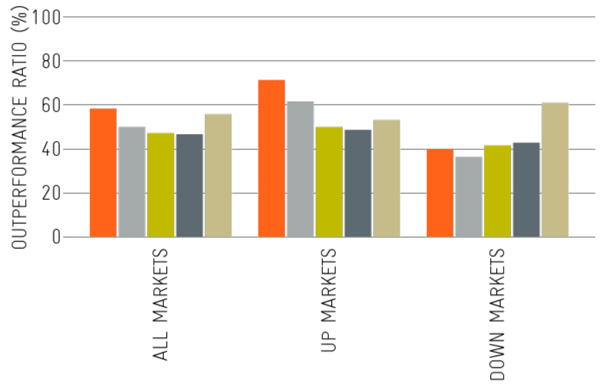
SMALLCO BROADCAP FUND
S&P/ASX 300 TR INDEX AUD
PEER MEDIAN
PEERS

Snail trail



START (07-2020) END (07-2023)

Outperformance consistency



1Y 2Y 3Y 5Y 10Y

Smallco Broadcap Fund

Glossary

Total return 'Top line' actual return, after fees

Excess return Return in excess of the benchmark return

Standard deviation Volatility of monthly Absolute Returns

Tracking error Volatility of monthly Excess Returns against the benchmark (the Standard Deviation of monthly Excess Returns)

Sharpe ratio Absolute reward for absolute risk taken (outperformance of the risk free return (Bank Bills) / Standard Deviation)

Information ratio Relative reward for relative risk taken (Excess Returns / Tracking Error)

Worst drawdown The worst cumulative loss ('peak to trough') experienced over the period assessed

Time to recovery The number of months taken to recover the Worst Drawdown

Snail Trail A trailing 12-month relative performance and relative risk measurement over the benchmark. The trail is generated using a 12-month rolling window over the specified period

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