



# Portfolio Update

April 2018

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# From the Directors

## April 2018 Review

April 2018 saw Australian equity markets, represented by the ASX 200, increase by 3.9% taking the calendar year to date return back to almost square at -0.1%. After 2 consecutive years of returns north of 11%, 2018 is certainly turning out to be more difficult for the Australian equity market. With the ongoing Royal Commission hearings, banks and financial services companies found the going tough. Globally we found developed markets out performing emerging markets during the month on the back of a strong US earnings season, however, over the calendar year we still note that emerging markets are 2% higher than their developed counterparts. Volatility remained in the market place with the historic Korean peace talks not quite removing the focus from US-Chinese trade relations and the looming spectre of a US-Russian conflict over Syria. Middle East instability saw the oil price up 7% and, importantly for Australia, iron ore was up 3.1% which made the weakness in the Australian dollar stand out even more. In the fixed interest space we saw 10 year US treasuries touch 3% for the first time in over 4 years.

### Australia

As Terry McMaster would likely attest after collapsing on the stand at the Royal Commission, all is not well with Australian banks and financial advisers. While no sectors detracted from the performance of the equity market during the month of April, the full year picture is markedly different. On a price basis, the financial services sector is down -6.8% after significant

fall out from the Royal Commission.

Having worked in the investment industry my whole career, I can say that the revelations of the past month do not come as a surprise. In fact, trying to run an independent boutique investment management businesses has been extremely difficult as a result of the corruption of the system. Financial planners have been driven, through regulation, to run high standard administration, compliance and investment research operations. Given that most planners tend to be small business the natural outcome was for planners to move to the big bank and insurer dealer groups. There they received administrative support through administration platforms, compliance support through dealer groups and investment research from independent research houses and asset consultants. I can tell you the banks have acted in their shareholders best interest and driven as much investment into in-house product as possible to the detriment of their clients.

How do we solve this issue? Given that most of the issues were originally brought about through regulation, well intended if not actually well executed, I highly doubt the best solution will be more regulation. I would posit that competition would be the best way to cure our ills. Unfortunately, we do not have a significant enough population to support competitive pressures. Given this, I would suggest that a number of high profile executives serving prison terms may be enough persuasion to cause people to behave properly.

An unintended fall out from the RC will be that the banks will now continue their withdrawal from lending markets with house finance a key risk. If banks make it tougher to obtain mortgages going forward then we will face a big issue given that Australian household debt continues to be among the worst levels in the world. It is no wonder consumer confidence declined to its lowest level since November of last year. While unemployment was steady, the number of jobs created was at 5,000 well down from 2017's averages. Inflation remains benign and given the above discussion, the RBA will find it difficult to raise rates any time soon.

### **Global Markets**

European equity markets were up 5.1% in April with strong retail sales growth at 1.8% year on year. The unemployment rate fell to 8.5% with Italy, France and Spain showing improvement. We would expect monetary policy between the US and the Eurozone to continue to diverge as their outlook for inflation diverges. There continues to be little expectation for inflation in the Eurozone with core inflation at 1%. The ECB still continues to provide accommodative monetary policy which is providing strong support for economic growth. Draghi has emphasised the need for "patience and persistence" and has indicated that the ECB will continue with its quantitative easing beyond September this year.

As discussed earlier, US 10 year treasuries hit 3% for the first time in 4 years but with the Fed expected to increase short rates 2 more times in 2018 the yield curve continues to flatten. Core inflation in the US has moved to 2.1% and wage inflation continues to concern market watchers at 2.7% year on year. Over two thirds of the S&P 500 Index have provided the market with their reports and we continue to see strong earnings per share growth of 29%. More than three quarters of companies that have reported have exceeded expectations. According to JP Morgan, one-third of the increase in earnings can be attributed to the tax cut, with one-third from higher domestic earnings and one-third from international earnings. The US equity market was however only up 0.4% for the month lagging its European counterpart. It was also below the Japanese market which returned 4.3% even though sentiment was hampered with global trade concerns weighing heavy alongside concerns on the currency. From a currency perspective the Euro has declined 1.8% against the U.S. dollar over the month while the yen declined 2.8% and the AUD rounded out the equation by declining 1.6% against the USD.

Yours Sincerely,

*Darren Katz*

Darren Katz,  
*Joint Managing Director*





## TAMIM Australian Equity All Cap Value IMA

The Australian equity market rebounded in April on the back of the resource sector. This was largely driven by commodity prices and Energy stocks led the way up 10.8% on the back of a 7% increase in the oil price. The laggard for the month was the financial sector, in particular diversified financials (-2.4%). This underperformance was driven by 19% fall for AMP on the back of revelations at the Royal Commission into the Banking, Superannuation and Financial Services sector. Our portfolio returned +2.5%, below the 3.5% for the market largely due to our cash weighting. The portfolio was boosted by strong returns from MSL Solutions (+18.4%), NetComm Wireless (+16.1%), Melbourne IT (+12.0%) and Horizon Oil (+11.5%).

### Portfolio News

Once again a number of the companies we hold announced positive news. In the current market where cheap stocks are hard to find we have focused on finding companies with identifiable catalysts whether they be potential acquisitions, new contracts or a step change in earnings. During the month we had one of each of those three scenarios play out.

**SRG (+7.0%)** announced the acquisition of TBS Group. TBS is a New Zealand based industrial contractor that specialises in asset and infrastructure maintenance services. The deal increases the proportion of SRG's revenues and earnings that come from services. The service revenue tends to have a greater recurring component than the construction work and hence we believe this acquisition was of strategic importance to the SRG business. In addition to the acquisition, we expect organic growth will continue to be strong as the company benefits from increasing infrastructure work in Australia. The

company currently has record work in hand and the immediate future looks strong. Another exciting aspect is the company's Joint Venture focused on dam repair in North America. This joint venture is not expected to add to earnings significantly in the near term but provides potential long term upside.

**NetComm Wireless (+16.1%)** announced an agreement with Bell Canada to supply them with their fixed wireless equipment for rural and semi-rural broadband. This deal adds to the existing agreements with the National Broadband Network and AT&T and shows that NetComm is slowly carving out a niche amongst the global telecommunications industry. We acquired a small position in the company after its most recent result which showed a significant swing in profitability. The company is well placed to win further contracts with leading global players and we look forward to further newsflow.

**MSL Solutions (+18.4%)** provided its most impressive quarterly update as a listed company with Operating Cashflow swinging into positive territory. The company also announced they are moving to monetise the holding of Zuuse on their balance sheet and have utilised some of the excess cash to make a small acquisition. Whilst its early days and our position in the company is a small one, the signs are positive. The company provides software solutions to clubs, stadiums, as well as sporting and golf associations. Growth for the company is coming via expansion globally as well as bolt on acquisitions.

## The Portfolio

The fund is currently invested in 21 companies. The cash level is currently 39.7% (down slightly from 40.6%). We trimmed our position in Gentrack whilst adding to positions in Trade Me, Global Construction Services and NetComm Wireless. Part of the current cash weighting is committed to a capital raising that will settle in May.

**GTK** 7.6%

**AXL** 4.7%

**HSN** 4.2%

**TME** 4.1%

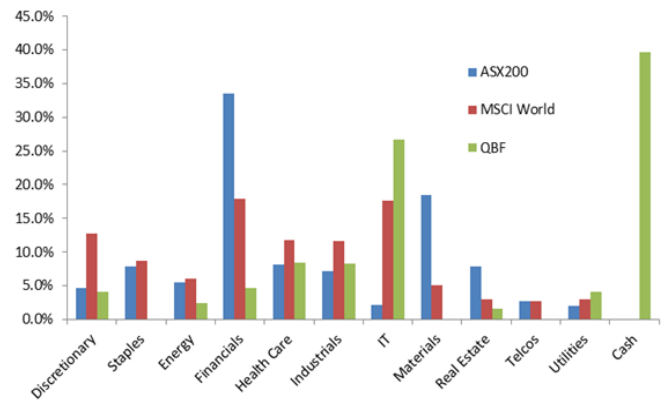
**DDR** 4.0%

**Other Positions** 35.8%

**Cash** 39.7%

## Sector Positioning

The fund maintains a strong overweight to the IT sector with other exposures in Healthcare, Financials, Industrials, Energy, Consumer Discretionary, Utilities and REITs.



# TAMIM Australian Equity Small Cap IMA



The TAMIM Australian Equity Small Cap IMA remains invested in the most compelling ASX listed micro-cap opportunities which are in our opinion both high quality and under-valued. The fund provides exposure to a genuinely differentiated portfolio of profitable companies, with bright prospects, and at attractive valuations. Correlation with the broader market remains low, and thus an investment in the small cap IMA is expected to bring diversification benefits to our shareholders' broader portfolios.

## Portfolio Review

The portfolio finished April weaker, with the key detractors being:

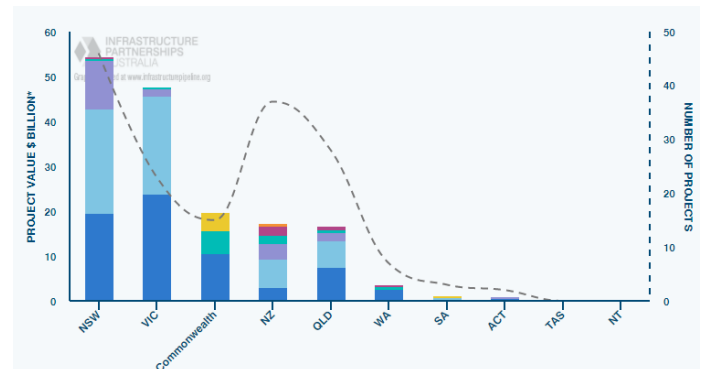
- **Zenitas Healthcare (ZNT)** – ZNT's share price continued to weaken during the month despite it confirming its FY18 expected EBITDA of \$13m to \$13.5m and announcing two accretive acquisitions. Management continue to deliver on their strategy and at month end, ZNT was trading on less than 9x FY19 earnings while the forward PE for healthcare stocks is currently approximately 29x earnings.
- **Konekt (KKT)** – during the month KKT advised it expected FY18 EBITDA of between \$8.5m to \$9.5m (previously expected \$10m, FY17: \$5.5m) with weaker workers compensation markets in NSW and South Australia impacting performance. KKT has forecast strong FY19 growth and is trading on less than 6x FY19 earnings and less than 4x pre-tax free cash flows. At these levels, given recent private equity and corporate activity in the sector, it represents an attractive takeover candidate.

Given their respective multiples, both stocks continue to offer meaningful upside so we will continue to focus on the long term opportunity.

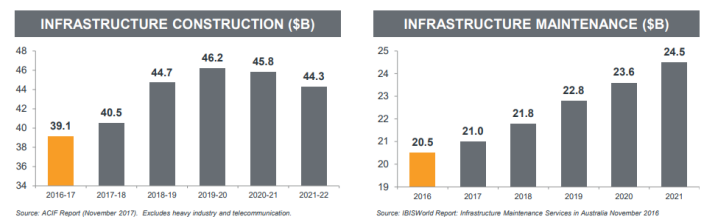
We continue to assess placements, capital raisings and sub-underwriting opportunities for the portfolio.

## Australia and New Zealand Infrastructure Exposure

The term “infrastructure boom” is often referenced in media commentary. While a “boom” may be somewhat overstating the significance, there is clearly an increasing amount of investment moving into infrastructure projects. Deloitte Access Economics notes that engineering and commercial construction activity increased by 12% in 2017, with a pipeline of over 150 major projects valued at over \$200 billion anticipated to come on line over the coming years.



This pipeline of new projects will support significant new construction and ongoing maintenance spend as outlined below for Australia.



Our challenge has been in identifying companies that have unique, market leading product/service offerings, that are well positioned to capture a meaningful portion of this spend, at attractive margins, while at

the same time having a diversified customer base so they are not exposed to any significant single contract risk. As always, we also require the investment to offer compelling valuation metrics. Over the last month we have increased our exposure to the infrastructure sector through further investments in two such companies that meet our strict criteria: **SRG Limited (SRG)** and **Traffic Technologies Limited (TTI)**. We recently published a more detailed write up on both of these stocks (found in the news section on the TAMIM website).

## Outlook

We continue to remain wholly focused upon what is within our control: executing on a well-considered,

time-tested, value-conscious investment philosophy.

We are enthused by the medium to long-term prospects across our current portfolio holdings. These are high quality businesses, with great management teams with whom we've built strong relationships. Importantly, pricing remains attractive; and ultimately will drive returns over time. We're working diligently to identify new holdings for the portfolio and are excited about the prospects of some names added to the portfolio in recent times. This constant renewal in the portfolio is important, with newly identified ideas being an important driver of long-term outcomes



# TAMIM Global Equity High Conviction IMA

## Market & Portfolio Review

The Strategy return for April 2018 was 3.9% in AUD terms, 1.1% ahead of the MSCI World Index. Value stocks outperformed Growth stocks. The last few years have favoured Growth stocks to the extent we now anticipate a return to favour of the Value style.

The Australian dollar retreated further against the USD despite strong positive commodity price moves.

Valero was amongst the biggest movers for April. Caterpillar fell as strong results were accompanied by a cautious statement on margins. We have made very few changes to our holdings in the last six months.

A Royal Commission investigating the provision of Financial Services in Australia has uncovered longstanding director and management ineptitude and multiple infractions of the law and internal procedures at the major banks and the AMP.

## Market Outlook

We are perhaps due for a market correction or at least a rotation from Growth. The behaviour of stocks is becoming more idiosyncratic and price moves are sharpening as volatility returns to normal.

As the USA yield curve flattens and the yield on the 10 year note has reached 3%, we would expect investors to focus upon debt loads and free cash flow. It is interesting to note the difference in performance between AT&T which is heavily leveraged vs Verizon which is not.

It is true that USA companies are showing record levels of profitability as measured by margins and 'profit share'. We favour stocks with plenty of room for improvement and a margin of safety.

We also remain fully invested in the model portfolio and unhedged for AUD based investors.



# TAMIM Income Fund

## Series 1

The Tamim Income Fund 1 generated an interest return of 0.72% in April and paid a 2% yield to investors at the start of May. The portfolio was allocated as follows:

Platform	Allocation
RateSetter	65.7%
Society One	30.6%
Cash	3.7%

The portfolio is currently invested into 2 loan platforms being the Ratesetter platform and the SocietyOne platform. The Ratesetter platform loans comprise 65.7% of the overall portfolio. It is important to remember that the Ratesetter platform operates with a provision fund which protects the portfolio loans to approximately the first 6% loss. This does however operate at a portfolio level so is not a guarantee of capital.

The Ratesetter provision fund balance is currently \$9,082,250 which is 5.96% of the outstanding loan book. Key Ratesetter details are summarised below:

### RateSetter Key Statistics

Key Statistics Since Inception	
Claims on Provision Fund	100% of late payments and defaults
Claims paid by Provision Fund	100% of total claim value
Total amount lent	\$275,188,677
Total principal repaid by borrowers	\$122,675,527
Current funds on loan	\$152,513,150
Current estimated bad debt rate*	<3.6%
Current estimated bad debt*	\$5,428,203
Current estimated default coverage ratio*	1.7x

Source: RateSetter

The SocietyOne loans comprise 30.6% of the overall portfolio and this is split across over 355 loans as follows:

Category	Allocation	Yield (gross)
A	18.9%	8.95%
B	29.8%	10.92%
C	46.7%	14.39%

**Data for Tamim Income Fund 1 Series 2 will become available from next month as most of the portfolio is now invested.**



The TAMIM Alpha monthly report aims to provide our investors with a general review of the Israeli market and describe the key events that occurred in the fund through the month of April 2018. We will be producing these reports on a monthly basis with a more in-depth report at the end of each quarter.

## Market Review

We would like to start by congratulating the State of Israel on its 70th anniversary. It is quite astonishing what has been achieved in such a relatively short time.

Some recent milestones reflect these achievements:

- The World Economic Forum's Global Competitiveness Report 2017-2018 ranked Israel 3rd in the world for innovation;
- Israel has the 3rd largest number of tech companies listed on the NASDAQ, behind only the US and China, and more than all listed European and Asian firms combined;
- In 2017, 112 Israeli tech companies were acquired for an amount equal to \$23 billion.

It is important to point out that a few of Israel's achievements in the past 70 years have been global, game-changing innovations. These include things like drip irrigation in the early 60s, the ubiquitous USB stick in the late 90s, the Waze GPS map and traffic navigation app in recent years and many more.

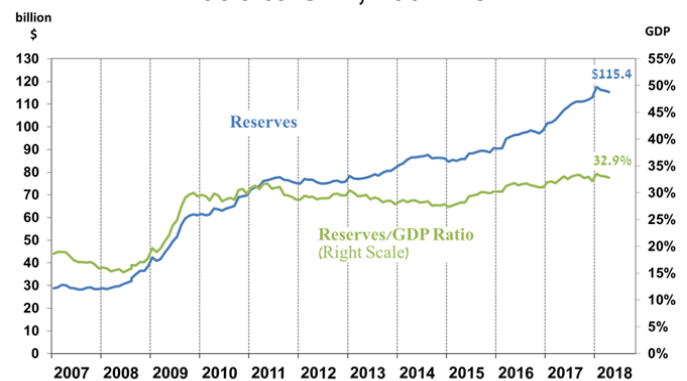
Back to the present, government activity amounted to a small fiscal surplus of NIS 0.5bn in April this year. This contrasts starkly to the last nine years in which the month of April registered a fiscal deficit. Furthermore, analysis of the data from the beginning of the year shows that in the first four months of 2018

(January – April), government activity amounted to a NIS 1.6bn deficit, compared to a higher deficit of NIS 2.9bn in the same period last year (see accompanying chart). Against this backdrop, we note that the cumulative deficit over the last 12 months ending in April this year equals NIS 23.5bn, or 1.8% of GDP according to Ministry of Finance estimates. This compares to a planned deficit of NIS 38.5bn (2.9% of GDP) for the full year

The Israeli shekel has depreciated nearly 5% against the USD and 4% against the EUR since the start of the year, providing a tailwind to Israeli exporters.

The foreign exchange reserves of the Bank of Israel have reached a record US\$115bn.

## Level of foreign exchange reserves, and their ratio to GDP, 2007–18



While writing this we are watching the President of the United States Donald Trump declare the immediate withdrawal from the nuclear agreement between the United States and Iran and a return to the imposition of economic sanctions. Of course, we cannot ignore this significant event and we do not know where this will lead to but in a practical sense there should be no

direct impact on our holdings in the fund.

We continue to implement our hedging strategy and are constantly seeking new investment opportunities.

## Portfolio Review

The month of April saw a continuation of the same momentum that we mentioned in the last quarterly report. This was characterised by two things in particular:

1. relatively high volatility;
2. Israeli equities with primarily global sources of revenue outperformed primarily domestically exposed Israeli companies.

As previously indicated, we have a number of strong examples of such companies in the portfolio. That is, the majority of their revenue is derived from outside of Israel. This includes anything from materials companies, like Israel Chemicals (ICL.TLV), to leading high-tech companies such as SolarEdge (SEDG.NASDAQ), Nova Measuring Instruments (NVMI.TLV) and Elbit Systems (ESLT.TLV & NASDAQ).

During the past month we have continued to increase our equity exposure mainly through increasing the position size of existing holdings, reaching 2.5-3% in each position. At month end we are at approximately 45% equity exposure. As we have increased our broad equity exposure during the past month we have accordingly increased our down side protection (put options). This will protect us from a decline of greater than 8% in the Israeli TA-125 index.

We have built a relatively sizable position in the renewable energy sector. In addition to our existing position in SolarEdge, we have initiated a position of 2.5% each in two companies: Enlight Renewable Energy (ENLT.TLV) and Energix Renewable Energies (ENRG.TLV). Both are companies that have great management teams and are on the verge of receiving significant additional projects. We believe that with an investment horizon of around two years these companies will provide significant value to our portfolio.

Renewable energy is a sector that Israel is already renowned for and is well positioned going forward with many cutting-edge and leading technologies or solutions in the marketplace.

The sector is growing and technology such as solar panels and wind turbines have matured, becoming cheap, efficient and accessible while the production of electricity is no longer dependent on government subsidies. This is a growing market globally and we could just be scratching the surface of this sector as an avenue for investment.

## Elbit Systems (ESLT.TLV & NASDAQ).



In this report we would like to focus on one recently initiated position – Elbit Systems (ESLT.TLV & NASDAQ).

Elbit Systems is a global high-tech company engaged in a wide range of programs throughout the world. They develop and supply a broad portfolio of airborne, land and naval systems and products for defence, homeland security and commercial applications. Today's growing worldwide defense, security and safety concerns have created the need for net-centric approaches to counter emerging, non-traditional threats. Forces, systems and platforms must be woven into an interoperable and joint network in order to succeed on the modern battlefield. Their systems provide customers with cost-effective capabilities to deploy all forces and responders on a networked basis, maximizing the potential for a powerful and coordinated reaction with speed, precision and intelligence.

Israel's defense exports reached a record number of US\$10bn in 2017 - an increase of 40% on the previous year.

The potential for the continued growth of Elbit comes in the form of a large deal that was announced just a month ago. Five years after plans were announced to privatize IMI Systems (Israel Military Industries), Elbit Systems will buy IMI for 1.8bn shekels (\$520 million). IMI Systems is a defence systems house specializing in the development, marketing and implementation of comprehensive combat-proven solutions for the land, air, naval and homeland security requirements of the modern battlefield.

With over eight decades of experience in the defense

of the modern battlefield.

With over eight decades of experience in the defense market, IMI Systems has a reputation as a preferred defense solutions provider and are positioned among the world's leading solution providers. They are a reputable IDF (Israel Defense Forces) supplier and a trusted provider of military and government agencies in over 70 countries worldwide including the U.S. military (Air Force, Army and Navy) and many other NATO nations. They offer state of the art artillery rocket systems, air to ground weapons and advanced tank and artillery ammunition.

The deal will create a company with a heavy emphasis on research and development, and whose product range will extend from IMI's shoulder-launched missiles, precision-guided mortar munitions and rocket-propulsion systems to Elbit's portfolio of avionic systems, drones and intelligence and cybertechnology.

We have recently concluded building two additional positions. The first being a technology company by the name of Nova Measuring Instruments (NVMI.TLV & NASDAQ) - a leading innovator and a key provider of metrology that designs, develops and produces monitoring and measurement systems for the semiconductor manufacturing industry.

The second position is in a company by the name of RADA Electronic Industries (RADA.NASDAQ). RADA is a defense electronics system house specialising in the design, development, production and sales of advanced electronic systems for airborne and land applications. RADA provides complete system solutions designed primarily for the aerospace and defense market.

We will elaborate on these investments in our next monthly report.

Sincerely,

Sagi Ben Yosef, Darren Katz  
& the combined TAMIM Alpha Team

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