Global High Conviction Portfolio

Individually Managed Account

Monthly Update

May 2019

TAMIM Asset Management
ABN 97 608 304 963 | AFSL 421469
1300 750 007

Global High Conviction
Portfolio Update

Robert Swift
Head of Global Equities
Portfolio Manager

Portfolio & Market Update

May was a negative month for global equities. We had thought 'sell in May and go away" would be the wrong advice but as it turned out that would have been profitable. We were defensively positioned but got hit.

The USA index, the S&P 500 fell nearly -7% and was the worst May performance for 50 years.

The cause was laid squarely at the feet of President Trump who escalated the dispute with China and opened two new fronts on the trade wars, with Mexico and Canada, being warned on the last day of the month that tariffs would be imposed if certain changes didn't occur. Prices in Lear Corp, Caterpillar and most industrials fell heavily.

This is political policy as if run by Caligula.

Meanwhile in dysfunctional Europe the elections to the EU Parliament showed marked dissatisfaction at current economic and social policy. We continue to think this market cheap but with dysfunctional politics and a cult following for the EU project and the Euro which borders on fanaticism which makes for dysfunctionality, the market will remain so. We continue to tell investors in Europe that they should do some reading into TARGET2 balances.

It didn't help that the yield curve went inverted with short rates higher than those at the long end. This is often a necessary but not sufficient requirement for a recession but we live in an 'Alice in Wonderland' economy at the moment with heavy government intervention in the price of money so who can tell what this means now? It seems unlikely that central banks will raise interest rates even if this monetary experiment of ultra-low rates is failing to ignite growth.

Many of the recent IPOs in the USA have been for loss making companies. The spread between Growth style returns and Value style returns is back to 1999 proportions. We are also telling investors that a return of 8%+ from equities from here is a great result and to favour quality balance sheets and valuation.

We prefer Asian risk assets including Japan to the USA to Europe and the UK.

Stock Spotlight: Discovery Inc.

Discovery
EXPLORE YOUR WORLD

Discovery Inc (DISCA.NASDAQ), formerly Discovery Communications, is the US media company that you are probably most familiar with through watching various documentaries on TV on channels like Discovery Channel, Animal Planet, Investigation Discovery, Eurosport, TLC, Travel Channel, the list goes on. It operates in over 220 countries and territories, and has over 300,000 hours of program library and produces 8,000 hours of programming each year. Discovery essentially focuses on making content and this is distributed through agreements with broadcasters, content platforms, and available over the internet through various providers etc.

There continues to be increasing consolidation in the media industry with Disney acquiring Fox while Comcast recently acquired Sky. The internet has been the biggest disruptor in recent years as companies such as Netflix and YouTube have taken eyeballs and revenue away from the incumbent players and so they have to respond either through new investment or more often, through acquisitions – it is easier, quicker and more likely to succeed.

Discovery itself made a big acquisition in 2018 of Scripps for US$14.6bn a business similar to itself focusing mainly on documentaries/real life content (HGTV, the Food Channel, Travel Channel). The reason for the acquisition was to combine costs and to distribute the Scripps content more internationally (before the acquisition Scripps content was only broadcast in Poland outside the USA), thus enabling group profits to rise further.

More media is being consumed online through Netflix and YouTube and this is posing a real headache for traditional distributors like TV broadcasters and cable companies. However, the one thing they all need is content to capture those eyeballs. Netflix so far has focused on making its own content for a unique offer, but this is proving extraordinarily expensive. As a rough rule of thumb, it costs US$5m an hour to produce scripted content (movies, dramas, etc) as opposed to US$400,000 an hour for the sort of content produced by Discovery. A lot more internet-based companies aspire to expand their media presence so they will need to make their own content or acquire it from the likes of Discovery, Disney, and the movie studio owners.

The problem comes if there are too many distribution channels (internet, broadcast TV, cable, etc) all showing pretty much the same programmes. So, companies are trying to focus on some form of exclusivity to ensure end consumers buy their platform. So recently we saw Disney, which produces wildly popular content based on Marvel comics, take back that content from Netflix. Actions like that obviously make distributors nervous because they don't have exclusivity and long-term security of content. There will continue to be a lot more mergers and takeovers in the media industry as a result of all this competition and a lot of it will center on the content companies of which there are very few that are still independent.

Following its big acquisition of Scripps at the beginning of last year, Discovery's biggest negative is its debt pile. Its total debt stands at US$14.5bn, Debt/Equity ratio stands at 190% and interest cover is 1.5x. The good news is that it is a very cash generative company and that its annual free cash flow is expected to be running at US$3.5bn+ so this high debt level should come down considerably over the next few years. It's valuation in terms of Price/Earnings ratio is very modest at 7.5x 2021 earnings reflecting its level of debt. This compares favourably to other media companies such as Walt Disney on 22x, Nine Entertainment on 13.5x, and Comcast on 12.5x.

We feel Discovery is a very interesting investment at these levels as profits are set to rise as cost cutting through combining the Scripps business comes through, selling the Scripps content in more countries and reducing debt as strong free cash flow comes in over the next few years. This should lead to a re-rating of the company's PE ratio and a substantial lift in the share price from $29 to over $40. The other possibility is that Discovery is taken over by one of the other media companies as the industry consolidation continues to take place.

Overview

The TAMIM Global Equity High Conviction IMA is a portfolio of global equities from major developed global exchanges. The portfolio holds approximately 25 of the best ideas from our investment manager's portfolios. The portfolio uses a systematic and consistent approach to stock selection and portfolio construction to deliver strong risk adjusted returns to our clients while focusing on attempting to preserve their wealth.

Key Facts

Investment Structure:	Individually Managed Account (only available to wholesale or sophisticated investors)
Minimum investment:	A$250,000
Pricing & Reporting:	Daily
Investment horizon:	3-5+ years
Management fee:	1.50% p.a.
Expense recovery fee:	Nil
Performance fee:	20% of performance in excess of hurdle
Hurdle:	RBA Cash Rate + 2.5%
Admistration fee:	Nil
Exit fee:	1% if exit within 12 months
Single security limit:	10% (typically 2-7%)
Benchmark	MSCI World Index
Target number of holdings:	20-30
Portfolio turnover:	< 25% p.a.
Investable universe:	ASX
Cash level (typical):	0-100% (5-10%)

Selection of 5 Holdings

Stock	Country
Verizon Communications Inc	USA
Legal & General Group PLC	UK
China Mobile	China
Macy's	USA
Ping An Insurance	China

Returns

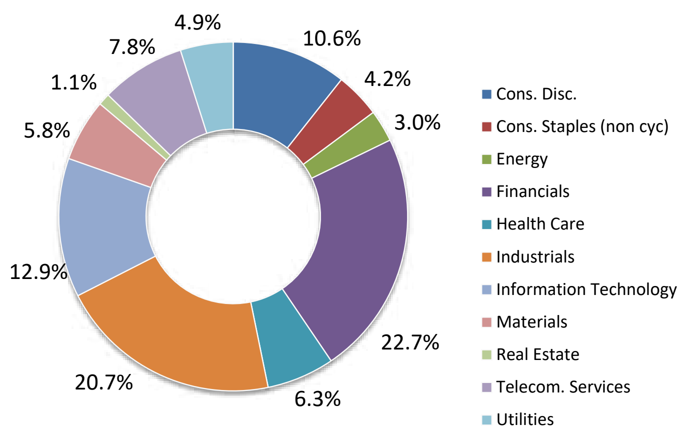
	1m	6m	1y	3y (p.a.)	5y (p.a.)	Since inception (p.a.)
TAMIM Glob. High Conv.	-6.28%	2.22%	-0.71%	4.68%	11.27%	14.42%
MSCI World	-4.27%	6.88%	8.89%	10.56%	12.20%	14.25%
Cash	0.12%	0.75%	1.51%	1.52%	1.80%	2.40%

Note: Returns are quoted net of fees and assume dividends are reinvested. Past performance is no guarantee of future performance. TAMIM Glob. High Conv. refers to the performance of the API High Conviction Strategy (Underlying Portfolio). The TAMIM Global Equity High Conviction IMAs mirror the Underlying Portfolio.

Portfolio Profile

Equities	97.2%
Cash	2.8%

Sector Allocation



Note: Portfolio returns are quoted net of fees. The ASX 300 refers to the S&P/ASX 300 Accumulation Index. Returns shown for longer than 1 year (other than Inception) are annualised. The information provided in this factsheet is intended for general use only. The information presented does not take into account the investment objectives, financial situation and advisory needs of any particular person nor does the information provided constitute investment advice. Under no circumstances should investments be based solely on the information herein. Please consider our Information Memorandum and Services Guide before investing in any of our products. Past performance is no guarantee of future returns. Returns displayed in this document are unaudited. For wholesale and sophisticated investors only.

Contact

Should you wish to discuss your investments or the various TAMIM solutions please do not hesitate to contact us:

Darren Katz
Managing Director
TAMIM
M 0405 147 230
E darren@tamim.com.au

Jeff Taitz
Managing Director
TAMIM
M 0403 444 040
E jeff@tamim.com.au

Disclaimer