SPHERIA ASSET MANAGEMENT

Spheria Opportunities Fund

ARSN 144 032 431 | APIR WHT0025AU | mFund SPM03

Performance as at 31st July 2022

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a[3]
Fund[1]	6.1%	-7.2%	0.9%	8.2%	9.8%	10.2%
Benchmark[2]	10.2%	-7.7%	-5.9%	5.9%	8.9%	8.8%
Difference	-4.1%	0.5%	6.9%	2.3%	0.9%	1.4%

1 Spheria Opportunities Fund. Returns of the Fund are net of applicable fees, costs and taxes.
2 Benchmark is the S&P/ASX Mid-Small Accumulation Index.
3 Inception date of the current investment strategy is 11th July 2016. The Fund was established in June 2010. Past performance is not a reliable indicator of future performance. All p.a. returns are annualised.

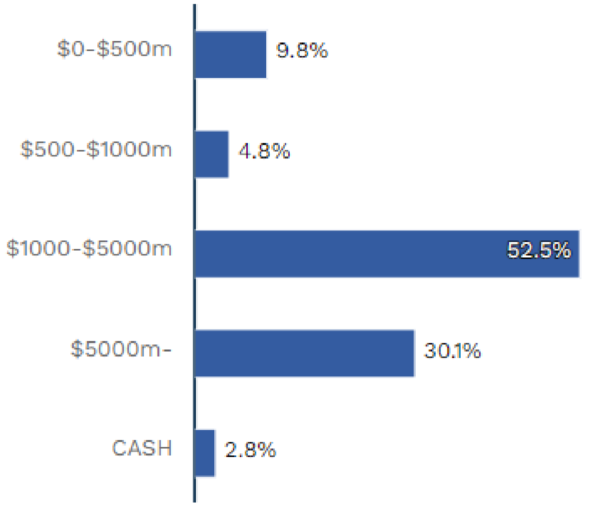
Overall Commentary

The Spheria Opportunities Fund returned 6.1% (after fees) during the month of July, underperforming the S&P ASX Mid-Small Accumulation Index by 4.1%.

Top 5 Holdings

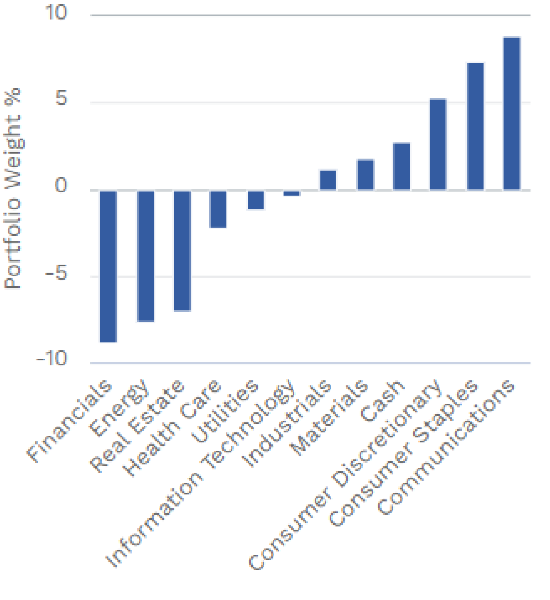
Company Name	% Portfolio
REA Group Ltd	6.6
The A2 Milk Company Limited	5.8
Alumina Limited	5.7
Incitec Pivot Limited	4.6
Orora Limited	4.5
Top 5	**27.3**

Market Cap Bands



Source: Spheria Asset Management

Active Sector Exposure



Source: Spheria Asset Management

Markets

The domestic small and mid-cap indices rallied strongly over July with both indices up over 10% for the month. The biggest driver of markets continues to be inflationary expectations and the flow through effects to long term (10-year bond) discount rates. Although inflation prints around the world continued to show year-on-year growth, there is an increasing expectation that the rate of change in inflation will likely slow. This makes some sense to us given a large part of the inflation base has been driven by energy prices and industrial commodities (Copper, Aluminium and Iron Ore to name the majors). Wage pressures however continue to rise as organised labour pushes for at least no real wage decreases in annual wage negotiations. Wages tend to lag actual inflation especially during volatile inflationary periods such as those we have just witnessed.

Whilst Central Bankers were doing their darndest to create inflation, having released the monster they are trying vainly to re-bottle it or at least contain it to target levels. It's not super surprising then that the Australian Government has announced a wide-ranging review of the RBA's objectives, the interaction of monetary policy with fiscal and macroprudential policy, including during times of crises. This is no small review. The Fed and ECB had the sense to do their own reviews without waiting for respective Governments to figure out the need. All have made some fairly drastic policy errors during the Covid crisis. The purchasing of 10-year government bonds by all must rank up there as one of the least necessary and most expensive unconventional acts. Having said that, the decline in 10-year bonds from around 3.65% at the end of June to circa 3% by the end of July, has started to chase away the bears. Over the month the best performing sectors were technology, healthcare and industrials with energy and consumer staples being the laggards. This was a turbulent rebound with investors picking up the pieces to put risk on. BNPL player ZIP Co (Z1P.ASX), Megaport (MP1.ASX) and Kogan (KGN.ASX) were the top gainers for the month in the Mid-Small index. ZIP and MP1 are not producing earnings let alone free cash flows.

Major Contributors for the Month

Due to the strong appreciation in the index the most significant attributions on a relative basis came from stocks not owned by the Fund that either declined in absolute terms or didn't rise as significantly as the index. Contributors here included Atlas Arteria (ALX.ASX) down 3.8% for the month, Ampol (ALD.ASX) down 2% over the month and Lynas Rare Earth (LYC.ASX) flat over the month. Positive contributions from stocks owned included:

Breville Group (BRG.ASX) – rallied 16% over July. BRG has been tarred with the consumer discretionary brush and whilst there some logic in this, it misses the fact that BRG is probably one of the most innovative and forward-thinking consumer appliance makers in the world. BRG has gradually been taking back distribution of its brands around various geographies (predominantly EU to date) and extending out its range. In the process, led by strong product, it has been outgrowing and thus taking share from its peer set. BRG remains tiny in the world of consumer appliances and yet has been investing well ahead of the curve to ensure its products are leading in term of their use to consumers. The group's philosophy has been to find useful ways of integrating technology for consumer benefit. For example, adding functionality that helps users create a desired outcome in terms of coffee or cooking rather than just linking up an appliance to the internet. BRG trades on a high teens EV/EBIT multiple one year forward but has a genuine global growth path a very high ROIC and an enviable track record of cash flow generation.

Seven West Media (SWM.ASX) – rallied 16% over July in sympathy with the market recovery. There was limited news flow out on SWM outside of their attempt to cancel their TV deal with Cricket Australia. The market has sold media names down aggressively over the past several months on the premise that a tough consumer environment would translate into much tougher media spending. Media names tend to be cyclical, and any downturn sees spending cuts. On the other hand, SWM has generated substantial cash since the last media spending downturn and goes into any potential cycle with a much-improved balance sheet. Valuation at SWM remains extremely compelling trading on an EV/EBIT multiple under 4x.

Regis Resources (RRL.ASX) – rallied 36% over July. RRL is a gold producer with stakes in two operating mines and one mine still in development approval. Despite reaching their production targets this year, costs have been impacted by high energy prices and the general labour shortage which has seen the shares sell off this year. Oil prices retraced from their peaks in mid-June which has improved sentiment in the energy intensive Gold sector. RRL has a virtually ungeared balance sheet and trades on extremely low free cash flow multiples. Whilst mine lives remain an issue for all gold companies including RRL, they have significant potential with the potential approval of McPhillamy's. Assuming limited development capex this year they balance sheet will return to a substantial net cash position.

Major Detractors for the Month

Due to the substantial recovery in the index, negative relative contributions came from many shares which were flat or which only modestly declined over the month.

Orora (ORA.ASX) – declined 2% in July on limited newsflow.

Bega Cheese (BGA.ASX) – declined 9% in July as cost pressures continued to weigh on sentiment for the company. We have detailed our views on BGA in the previous monthly report but in short, we believe the current share price is capitalising the current challenging (and cyclically low) conditions in which BGA finds itself. Whilst BGA does carry some debt on its balance sheet post the LDD (Lion Dairy Drinks) deal, the business has gone through a substantial investment in its capital base and will generate decent cashflows in this downturn. As raw materials cost pressures eventually abate, we expect to see substantial recovery in the earnings base of BGA.

Flight Centre (FLT.ASX) – was essentially flat over July despite a material upgrade (reduction in forecast loss) to its earnings guidance for FY22. FY22 is still a recovery year for FLT but each quarter has seen successive improvement in the level of travel globally. FLT's H2 is now expected to be running at break even on an underlying basis. Both their corporate travel and retail businesses are seeing strong recoveries although these are being somewhat hampered by logistical issues with the airlines. Staff shortages due to illness and unpredictable travel demand have somewhat reduced the total travel spend although against this there has been a strong increase in ticket prices which has aided FLT. One of the key peculiarities about travel stocks is their working capital movements, as their top line recovers, cash flows materially improve as they charge customers up front and retain this working capital until they are required to pay airlines (in a short time frame) and hotels (over a longer time frame which can be up to 2 months).

Outlook & Strategy

Market volatility is a reaction to the unusual global times we find ourselves in. The world markets are coming to terms with an end to huge government stimulus programs and record levels of QE intervention from Central Banks. Throw extremely high short term inflation numbers into the mix and the market gyrations almost make some sense. Although the yield on Australian 10-year bonds have compressed materially over the past 6 weeks (from around 4.2% at their peak in mid-June to around 3.0% at the end of July) we believe we have entered an era of higher rates and higher inflation than that of the past decade. This will mean valuation centric investors and those paying heed to fundamentals are more likely to outperform. The market has already rotated out of aggressively cash burning businesses and we still expect to see some further rationalisation as wary investors remain reluctant to throw additional capital at these companies.

Platform Availability List

If a fund is not available on your preferred platform, please contact us.

Please check with your platform for minimum investment requirements and fees.

FNZ Group

HUB24

mFund

Praemium

Macquarie Wrap

Spheria Opportunities Fund	
Benchmark	S&P/ASX Mid-Small Accumulation Index
Investment Objective	Outperform the S&P/ASX Mid-Small Accumulation Index over the medium to long term
Investing Universe	Primarily listed companies outside the top ASX 50 listed companies by market capitalisation and companies listed on the New Zealand Stock Exchange with an equivalent market capitalisation
Holdings	Generally 20-65 stocks
Distributions	Half-Yearly
Fees	0.99% p.a. Management fee & 15% performance fee of the Fund's excess return versus its benchmark, net of management fee.
Cash	Up to 20% cash, typically 5% - 10%
Expected Turnover	30% - 40%
Style	Long only, risk aware
APIR	WHT0025AU
Minimum Initial Investment	$25,000

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Fund Ratings

Further Information

For more information, please contact Pinnacle Investment Management Limited on 1300 010 311 or email distribution@pinnacleinvestment.com

Disclaimer