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Ausbil MicroCap Fund

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Quarterly performance update

December 2023

Returns[1] as at 31 December 2023

Period	1 month	3 months	6 months	1 year	2 years pa	3 years pa	5 years pa	7 years pa	10 years pa	Since Inception pa[2]
Fund return %	3.62	5.12	7.41	1.69	-10.94	4.32	12.67	11.43	13.69	18.96
Benchmark[3] %	6.47	5.34	-0.21	-0.36	-12.13	3.54	13.06	8.22	8.00	4.30
Out/under performance %	-2.85	-0.21	7.62	2.04	1.19	0.78	-0.39	3.21	5.69	14.66
Reference Index[4] %	7.23	8.52	6.42	7.82	-6.19	0.95	6.40	5.91	6.01	4.39
Out/under performance %	-3.61	-3.40	0.99	-6.14	-4.75	3.38	6.27	5.52	7.68	14.57

‘Leading inflationary and employment conditions have continued to soften… a welcome reprieve for the small and micro-cap sector outlook’

Performance Review

Fund performance for the quarter ending December 2023 was +5.12% (net of fees) versus the benchmark return of +5.34%, as measured by the S&P/ASX Emerging Companies Accumulation Index, and the reference index return of +8.52% as measured by the S&P/ASX Small Ordinaries Accumulation Index.

2023 will be remembered as the most anticipated recession in history, which of course never eventuated. Significant rate hikes, initially a source of concern, were balanced by a robust labour market and moderating inflation, providing thus far the cushion for a soft landing.

Returns for the year were concentrated in large caps[5], returning +12.7% for the year, relative to Australian microcaps[3], that ended the year broadly flat. The Fund returned a modest +1.70% (net of fees) for the year, improving notably in the second half of 2023 with a +7.41% return (net of fees). Strong performances from Tuas (+140%), Genesis Minerals (+43%), MMA Offshore (+67%), Life360 (+56%) and Temple & Webster (+116%) underpinned returns, while the Fund primarily recorded weakness in resources investments.

For the quarter, expectations of a Fed pivot fuelled the market for a strong run into Christmas. The Fund’s quarterly performance was broadly on par with the benchmark, achieving a +5.12% return (net of fees) compared to the benchmark’s +5.34%.

The Fund ended the year with 35 positions, a top-10 concentration of 46%, and less than 4% cash. As we enter 2024, we have been increasing our conviction that lower nominal interest rates and stabilising inflation will create favourable conditions for small and micro-cap companies to thrive following a prolonged period of underperformance relative to larger companies.

This quarter, the largest positive contributors to performance were Tuas and MMA Offshore. Negative contributors included Karoon Energy and Johns Lyng Group.

Key Contributors

Tuas (TUA) returned +50.2% following a strong trading update at the December AGM. TUA has been rapidly expanding its mobile business through simple and competitive plans, with subscriber growth at the 1Q24 result up 37% yoy. With less than 10% penetration of the Singapore mobile market, we believe there is ample runway for future market share gains. This founder-led company is leveraging its success to broaden its reach as a holistic challenger in the telecommunications sector, enhancing its 5G coverage and branching into broadband, business, and enterprise services.

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MMA Offshore (MRM) returned +34.5% over the quarter following a substantial earnings upgrade at its November AGM. Robust demand across oil and gas services, combined with limited new vessel supply, has put upward pressure on vessel leasing rates. We remain vigilant not to be caught naked as the tide goes out, however with a lack of new vessel supply growth, and an insufficient incentive price to stimulate more supply, we believe these conditions will sustain this growth cycle for some time yet.

Key Detractors

Karoon Energy (KAR) fell -22.4% over the quarter. KAR announced a capital raising and acquisition of a non-controlling interest in the Who Dat field in the Gulf of Mexico, diversifying its production base beyond offshore Brazil. The new asset offers high-quality, low-cost production in a Tier-1 jurisdiction. Despite the unfavourable timing coinciding with a drop in oil prices, the acquisition presents multiple opportunities for near-term development and exploration.

Johns Lyng Group (JLG) fell -6.3% over the quarter. JLG reconfirmed guidance at the November AGM, possibly leading to disappointment among some market participants expecting an upgrade even though historically the company’s AGM has not typically featured guidance updates. However, we believe that the earnings outlook remains positive. Recent severe weather events in North and South-East Queensland are likely to bolster JLG’s catastrophic weather event and make-safe services, and support its catastrophe backlog of work. JLG has been one of the most successful investments realised for the Fund since inception, with the position established in May 2019 at around $1.35 per share. Following a period of graduation into the S&P/ASX 200, the company is now firmly in the sights of the small and mid-cap universe.

Outlook

Leading inflationary and employment conditions have continued to soften, and along with ongoing geopolitical tensions, it is likely that central banks will continue to ‘jawbone’ their stance, erring on the side of caution. Entering 2024, the direction for interest rates will likely be down although the timing will be data dependent. This should remain accommodative for equity markets, coupled with slowing growth globally, and a welcome reprieve for the outlook of the Australian small and micro-cap sector.

Top 10 Stocks[6]

1. Boss Energy
2. Genesis Minerals
3. Imdex
4. Jumbo Interactive
5. Life360
6. Light & Wonder
7. Macquarie Technology Group
8. MMA Offshore
9. Propel Funeral
10. Tuas

1. Fund returns are net of fees and before taxes.
2. Date: February 2010.
3. S&P/ASX Emerging Companies Accumulation Index.
4. S&P/ASX Small Ordinaries Accumulation Index.
5. S&P/ASX 100 Accumulation Index
6. Top 10 stocks sorted alphabetically.

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