Evans and Partners International Fund

JUNE 2019 QUARTER REPORT

For fund investor use only. The views expressed herein are part of a wider portfolio investment strategy and should not be considered in isolation.

PERFORMANCE TO 30 JUNE 2019

	3 MONTHS	6 MONTHS	1 YEAR	3 YEARS (P.A.)	5 YEARS (P.A.)	SINCE INCEPTION (P.A.)
Portfolio return (AUD)	11.3%	26.3%	27.4%	15.7%	16.5%	14.9%
MSCI AC World Accum Index ex-Aust (AUD)	4.8%	16.5%	11.3%	13.9%	12.8%	12.2%
Excess return	**6.5%**	**9.8%**	**16.1%**	**1.9%**	**3.7%**	**2.7%**

Performance is net of investment management fees. Inception date is 18th February 2014. Numbers may not sum due to rounding. Since inception return is annualized and assumes reinvestment of distributions. Past performance should not be taken as an indication of future performance.

BOB DESMOND
Head of International Equities

ADAM CHANDLER
Portfolio Manager

CONTRIBUTION TO PORTFOLIO RETURN – QUARTER JUNE 2019 (%)

TOP THREE		BOTTOM THREE	
adidas	2.12	Alphabet	-0.64
TE Connectivity	1.31	Compass	0.19
Equifax	1.20	Booking Holdings	0.33

Numbers represent contribution in percentages of each stock to the percentage change in portfolio value.

SECURITIES MOVEMENTS FOR THE QUARTER OF JUNE

Bought in	Booking
Sold out	Experian
Increased holding	Aon, Ross Stores, Alphabet, Nordson, Compass
Decreased holding	CDW, LVMH, Sika, Accenture, adidas

TOP FIVE HOLDINGS AS AT 30 JUNE 2019

	REGION	SECTOR
Visa	US	Financial Services
Alphabet	US	Technology
Aon	US	Financial Services
Equifax	US	Financial Services
Ross Stores	US	Consumer

MARKET COMMENTARY

International equity markets appreciated by 4.8% over the June quarter (all figures are in AUD unless noted otherwise). Despite a steep fall in May as concerns built around the US-China trade war, stock markets rebounded in June, supported by signalling from key central banks regarding an easing of monetary policy. The Australian equity market outperformed global equities, increasing 8.6% for the quarter.

The US equity market increased 5.4% over the quarter, setting a new record high for the S&P 500. The US 10-year bond ended the quarter at 2.0%, down from 2.4% at the end of the March quarter, and this has been broadly supportive of equity valuations.

European equity markets appreciated 5.8% in the first quarter. Markets exposed to trade, such as semiconductors and automotive, fluctuated as trade talks progressed. Mario Draghi, the European Central Bank President, suggested that further monetary easing could be expected if the inflation outlook fails to improve. UK equities were up 2.2%, despite ongoing Brexit concerns, which have clouded the economic outlook for an extended period.

Emerging markets equities increased a moderate 1.8%, led by Russia (+18.3%) and Brazil (+8.5%). The Central Bank of Russia cut interest rates by 25 basis points to 7.25% in June, signaling potential for further easing. Chinese equities closed the quarter down 2.8%, impacted by ongoing trade tensions. A US-China tariff truce, agreed last December, expired in May and the US increased tariffs on $200bn of Chinese imports, from 10% to 25%, while also effectively blacklisting Chinese telecoms provider Huawei (the US have since eased export controls on the company). The Chinese government retaliated by raising tariffs on $60bn of US exports. Subsequently, President Trump indicated that consideration was being given to further tariffs on the remaining $300bn of Chinese imports. In June, negotiations became more constructive, as President Xi and President Trump agreed to restart trade talks at the G20 summit.

The performance of all sectors was positive over the June quarter. Financials (+7.1%) posted the strongest gains, closely followed by Information Technology (+6.5%). The Energy sector (+0.1%) was the worst performer, while the Healthcare sector (+2.5%) remains challenged by potential US legislative changes.

PORTFOLIO PERFORMANCE

The Evans & Partners International Fund appreciated 11.3% for the quarter, outperforming the broader market by 6.5%.

Key contributors to performance for the quarter were **adidas** and **TE Connectivity**:

- **adidas** – the company reported a strong first quarter result, with EPS growth of 19%, primarily driven by margin improvement. Earnings were c.10% ahead of consensus expectations, with adidas' overall growth trajectory benefiting from continued momentum in greater China (+16%) and e-commerce (+40%). Enhancements in their channel mix are driving gross margin expansion and management is continuing to improve operating leverage. The ongoing strengthening of the company's fundamentals have resulted in more favourable investor sentiment towards adidas.
- **TE Connectivity** – after a more challenging end to 2018, the company's share price appreciated over the quarter as our investment thesis continues to play out. TE's 2Q19 result saw adjusted EPS come in flat year-on-year; ahead of both management's guidance and consensus expectations. We are encouraged by the solid order pipeline across all three divisions, signaling a recovery in some of their key end markets. Pleasingly, management revised up FY19 guidance by c.4% following the improved profitability in 2Q19.

The notable detractor from the portfolio was **Alphabet**:

- **Alphabet** – the company reported its 1Q19 earnings, with revenue growth of +17% (+19% in constant currency). The top line came in 3% lower than the market anticipated, resulting in a brief sell-off and an 8% fall in the share price following the result. During the quarter there were also some market concerns around a potential anti-trust investigation. We have done extensive due diligence with legal experts and at this stage we believe the market is overstating these risks. We will continue to monitor the situation. Ongoing strength in mobile, Google Cloud, and YouTube reaffirmed our view on the company's longer-term growth prospects and competitive advantage. We expect investment spending growth will moderate, which will assist profitability over the medium-term.

PORTFOLIO CHANGES – STOCKS ADDED TO THE PORTFOLIO

Booking Holdings (BKNG) – Booking is the world's leading Online Travel Agency (OTA). The company provides a network offering hotels exposure to a global audience (booking.com is the world's most visited travel website) and provides customers with a wide choice of accommodation (c.2.2m properties in 230+ countries) and services through a user-friendly platform. Through its appealing asset-light platform business model, industry leading IT capabilities and scale, Booking has grown EPS by c.20% p.a. on average over the past five years. High profitability (~39% EBITDA margin compared with its key competitor and the 2nd largest OTA, Expedia, at c.18%,) allows Booking's long-term focused management to reinvest into the business and continue to expand its competitive moat.

Booking's underlying growth is supported by strong industry growth (at c.2x GDP) and by the ongoing shift from offline to online bookings. Rapid expansion into alternative accommodation (homes) has also been a key growth driver (c.20% of revenue in 2018, matching Airbnb's revenue). There are significant opportunities for growth, as Booking has <10% share of the accommodation market. Substantial investment in advertising (c.$6bn, or 40% of sales in 2018) guarantees top ranking in the key search channel (Google), making it hard for hotels to bypass Booking, while also improving brand equity and direct traffic (>50% of reservations are done directly on booking.com or the app).

Over the next three years, we forecast revenue growth of c.8%, flat margins and buybacks of c.5% p.a. to drive EPS growth of c.13%. At the time of our initial investment, Booking traded at 17.7x our one-year forward EPS, representing a 5% premium to the S&P 500 compared with a historical premium of approximately 20%. While we appreciate Bookings' growth profile will moderate from historical levels, we believe the current multiple is not reflective of the underlying business quality (dominant player, strong management, net cash position) and potential for growth re-acceleration from ongoing incremental investments.

PORTFOLIO CHANGES – STOCKS REMOVED FROM THE PORTFOLIO

Experian (EXPN) – we sold our remaining position in the company based on valuation considerations. Whilst we still consider this a high-quality business, at the time of disposal it was trading at 27x next-twelve-month earnings and a 16% premium to our estimated valuation.

COMPOSITION OF PORTFOLIO PERFORMANCE

	3 MONTHS	6 MONTHS	1 YEAR	3 YEARS (P.A.)	5 YEARS (P.A.)	SINCE INCEPTION (P.A.)
Local currency impact	10.1%	25.9%	23.6%	13.6%	11.1%	10.8%
+/- currency impact on return	1.2%	0.4%	3.7%	2.1%	5.4%	4.1%
Portfolio return (AUD)	**11.3%**	**26.3%**	**27.4%**	**15.7%**	**16.5%**	**14.9%**

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PORTFOLIO CHARACTERISTICS – 3 YEARS TO JUNE 2019

Standard deviation	11.7%
Realised beta	1.05
Tracking error	5.9%
Upside capture ratio	1.11
Downside capture ratio	1.00

FUND NAME	EVANS AND PARTNERS INTERNATIONAL FUND
APIR Code	ETL0390AU
ARSN	166 708 792
Responsible Entity	Equity Trustees
Number of stocks	10 - 15
Maximum cash weighting	10%
Maximum single stock weighting	10%
Currency exposure	Unhedged
Benchmark	MSCI All Countries World Accum Index ex-Australia (AS)
Minimum Investment	$20,000
Distribution Frequency	Bi-annually
Investment Management fee	1.25% incl. GST
Buy/sell spread	0.10% / 0.10%
Fund Inception	18th February 2014

IMPORTANT INFORMATION