

SUMMARY

February performance was -7.6% versus flat for the Small Ords Accumulation index taking since inception returns to 17.4% p.a.

COMMENTARY

Small Resources +7.6% materially outperformed Small Industrials -2.3% in February. Two of our biggest sector overweights are Information Technology and Communication Services which fell -12.8% and -4.7% respectively. Elsewhere, sectors in which we have no weight such as Energy and Materials rose +10.2% and +7.1%. This made for one of the most challenging reporting seasons we can recall.

The valuations of many of our holdings have compressed in anticipation of higher rates due to fears of persistent inflation. While higher interest rates impact the valuation of longer-dated cash flows, we believe our portfolio is well placed to deal with higher inflation should it persist. In an environment where inflation persists, we'd much rather own companies with growth and pricing power; as these are the companies that will sustain their earnings in real terms. We are sceptical of the view the best way to navigate inflationary times is by owning lowly-rated, low-growth companies without pricing power; we think the opposite is true.

When we think about markets in the short-term the F1 commentator Murray Walker probably sums it up best; "anything can happen, and it usually does." However, over the long-term we know prices follow fundamentals. In times of market stress, it is worth getting back to basics; share prices follow earnings. A phrase often heard around the QVG offices is that we're looking for "organic free cash flow per share growers" (we don't get out much). Almost all the truly great high-performance companies share this characteristic of strong multi-year free cash flow growth.

Uniti Group, Trajan, Imdex, IDP Education and MA Financial fell anywhere from -5% to -21% for the month despite posting results in-line or ahead of expectations. It is clear the market currently prefers large cyclical companies such as banks and resources. Small industrial growth companies are being sold to fund these purchases. [Note: We have seen this before. A vivid example was November 2016 when Trump unexpectedly won the Presidency, and his promise of tax cuts and stimulus saw a flood of money into large cyclical companies at the expense of smaller ones. This led to a similarly weak period of absolute and relative performance.]

The fund was also impacted by **City Chic**, **Tyro** and **BWX** which fell -31%, -26%, -26% on the day of their results. The downwards earnings revisions for these companies meant some share price fall was to be expected. We always make mistakes, and can't promise not to in the future, but the magnitude of market response to these errors was a surprise.

This is the fifth significant drawdown we've seen in our history of managing money and, while painful, they do provide opportunities. Inflation, rates and war are front of mind for all market watchers. In response to these risks, our approach is to stick with the process and stay invested in the best businesses we can find. This process of finding lowly geared, high return on capital business has served us very well in the past and find it hard to believe this approach will stay out of favour forever.

We remain optimistic

The start to 2022 has been very difficult for investors who favour growth stocks. Despite a gloomy market for our style, we remain excited by the prospects for the portfolio. This conviction has seen us add meaningfully to our personal investment in the fund in January and February. Of course, we have no idea whether there is more pain to come – and take a 3 year plus view when making such investments – but we do know over the long-term companies that can sustainably compound earnings at high rates of return will triumph.

NET PERFORMANCE

PERIOD	FUND RETURN	BENCHMARK RETURN	OUT / UNDER-PERFORMANCE
1 month	-7.64%	-0.01%	-7.63%
1 year	+5.75%	+5.02%	+0.73%
Since Inception	+105.46%	+48.30%	+57.16%
Since Incept p.a.	+17.37%	+9.16%	+8.21%

TOP 5 HOLDINGS

1. Uniti Group (UWL)
2. Johns Lyng (JLG)
3. Hansen Technologies (HSN)
4. HUB24 (HUB)
5. Imdex (IMD)

THE MANAGER

QVG Capital is an independent boutique investment management company managing funds on behalf of high-net-worth individuals and institutions ("wholesale investors"). QVG was established in June 2017 by Tony Waters and Chris Prunty and is wholly owned by its staff. QVG manages a long-only small companies fund – the QVG Opportunities Fund – and an all-cap absolute return fund – the QVG Long Short Fund.

QVG's FUNDS

QVG Capital manages the **QVG Opportunities Fund**; a 'best ideas' fund focusing on smaller companies and the **QVG Long Short Fund**; an all-cap absolute return fund. The Opportunities Fund predominantly invests in Australian-listed smaller companies; defined as those outside the S&P/ASX 100. The Opportunities Fund is closed to new investors while the Long Short Fund is open to new and existing



TONY WATERS

Tony has 30 years experience in financial markets most recently as the Portfolio Manager of the Ausbil Micro Cap Fund from its inception until April 2017. Tony joined Ausbil from Investors Mutual in 2008. Before that he spent 9 years as a small cap analyst at institutional stockbroker CCZ.



CHRIS PRUNTY, CFA

Chris has 19 years experience in financial markets most recently as the Co Portfolio Manager of the Ausbil Micro Cap Fund having joined Ausbil at the inception of the fund in February 2010. Prior to Ausbil, Chris was an analyst researching smaller companies at Investors Mutual, Confluence Asset Management and CCZ Equities.

OUR APPROACH

TRACK RECORD The managers have a long association having worked together for over a decade at three previous firms; CCZ Equities, Investors Mutual and Ausbil Investment Management where they were Portfolio Managers of the award-winning Ausbil Micro Cap Fund.

ALIGNMENT Our personal investment in the fund means there is a high degree of alignment between our investors and ourselves. The principals do not buy Australian-listed companies outside the fund.

PHILOSOPHY & PROCESS Our philosophy and process has been refined and tested over a decade and has stood the test of time in the small companies space in Australia. An earnings focus with quantitative measures of quality and value and our experience combines to generate a portfolio of undervalued growth companies in the process of being discovered by the market.

CAPACITY MANAGED The fund has been designed to mitigate the liquidity risk of investing in small companies. The manager is aware that too many assets under management impacts performance and will seek to actively manage capacity with maintaining performance the key objective. The fund closed to new investors on August 1, 2018.

FUND INFORMATION			
Name	QVG Opportunities Fund	Investor Eligibility	Wholesale or 'sophisticated' investors only
Structure	Wholesale Unit Trust	Minimum Investment	\$250,000 (unless otherwise agreed)
Investment Universe	ASX-listed smaller companies	Liquidity	Daily Unit Pricing Applications and Redemptions
Benchmark	S&P/ASX Small Ords Accum	Fees	1.2% management and 20.5% performance
Stock Holdings	29	Admin & Custodian	Link Fund Solutions
Stock Limit	10% at cost	APIR Code	QVG9204AU
Trust FUM	\$635m	Platform Availability	Netwealth, HUB24, AUSMAQ, POWERWRAP

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