

REPORT TO THE UNIT HOLDERS IN THE ASPIRING FUND FOR THE  
MONTH JULY 2018

	Aspiring Fund	NZ50G	ALL Ords Accumulation Index (rebased in NZ\$)
<u>Short-term returns</u>			
Month	0.27%	-0.24%	1.29%
Last 3 Months	5.16%	5.67%	7.70%
Last 12 Months	12.11%	15.96%	17.84%
Financial Year to Date	7.40%	7.25%	12.31%

Long-term\* returns and volatility

Return (annualised)	10.91%	7.04%	3.36%
Return volatility (annualised)	8.56%	11.31%	16.11%

\* since the introduction of the PIE Tax regime, 30 Sept 2007

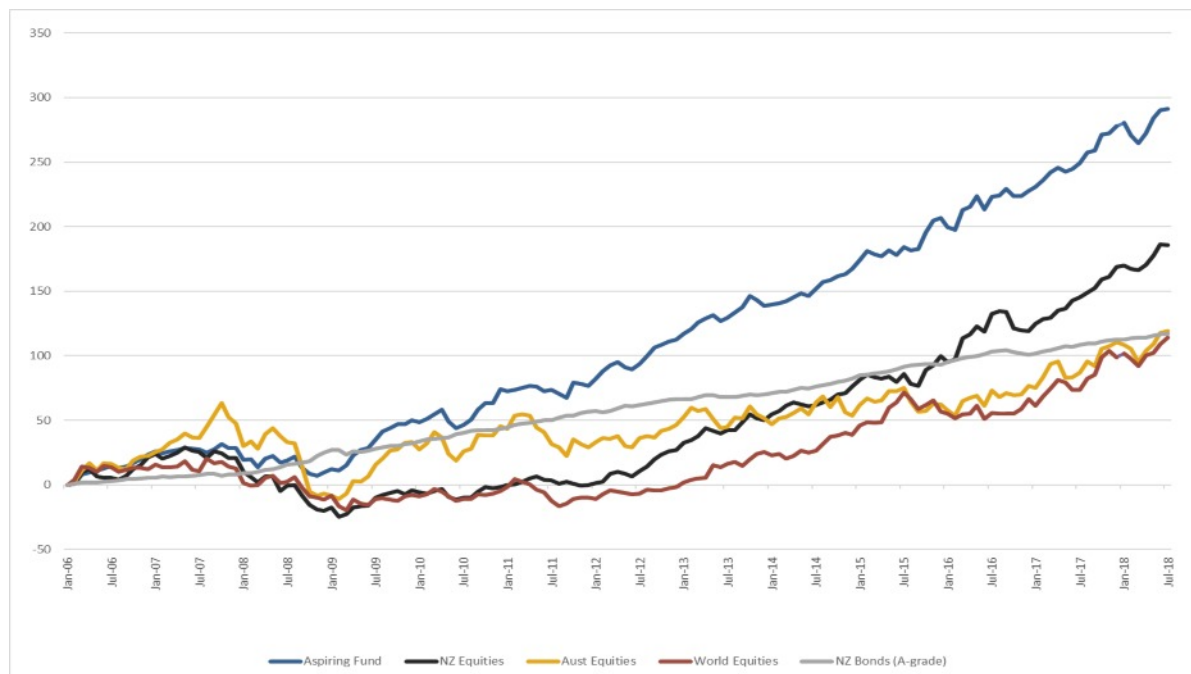
Unit Price \$3.66

**ASSET ALLOCATION (approximately):**

New Zealand Equities	35.7%
Australian Equities	20.0%
International Equities	7.4%
Bonds	4.0%
Total Cash	32.9%
Short Equities	-0.4%

**Net Asset Value of the Fund (approximately):** 408.7m

# Fund Performance



The Fund returned 0.27% in July with strong performances from EBOS and the international portfolio offset by a flat performance from the remainder of the portfolio.

July was low on news and deal flow in Australasia with schools on holiday for much of the month and reporting season starting in August. We did get another weak reading from NZ businesses with the publishing of the ANZ Business Outlook survey. According to ANZ, this was the weakest business outlook since halfway through the post-GFC recovery. This confirms our view that NZ Inc. is well past its peak and remains uncertain about the future under the new government. We have been reducing our exposure to the NZ market for some time and expect a fairly cautious outlook from companies reporting in August.

The Fund's best performer was EBOS, up 12.5% after announcing it had won the exclusive distribution of all pharmaceutical products for Aussie's largest pharmacy retailer, Chemist Warehouse. The contract, starting mid-next year, is expected to generate ~ A\$1b in sales (~12% of group revenue), and lifts EBOS's share of the pharmacy wholesale market for pharmaceutical products to 40-45%.

The contract win is unequivocally positive for EBOS, with its increased scale affording it cost advantages over its competitors, and as it saddles up to the dominant player in the market, who continues to win market share. EBOS has long been lauded for its strong executive team who have done an excellent job of managing shareholder capital and becoming the market leader in operational efficiency, in a difficult industry due to its thin margins and regulatory oversight. This win is another feather in the cap of one of NZ's best companies and the stock re-rated to what we consider to be a fair valuation.

EBOS won the contract off Sigma Pharmaceuticals, whose stock fell 40% on the announcement, approximately in line with the anticipated earnings impact. It will be interesting to see how aggressive Sigma will be in going after new business to fill its significant spare capacity, however EBOS's well diversified customer base should serve it well in this regard.

The ASX200 had another reasonable month finishing up 1.4% in A\$. While ahead of our portfolio it was noteworthy that there appeared to be some rotation back into large cap stocks, with the Banks and Telstra driving a lot of the move. As previously highlighted we believe the Banks face a challenging credit, cost and compliance outlook while the competitive landscape and pricing outlook for Telco's looks tough to say the least, hence we have no exposure to these sectors.

For our portfolio the highlight was waste management company Cleanaway (+10%), now a top 100 stock gaining traction with investors after the Tox acquisition, multiple contract wins, and increasing familiarisation with management. While not cheap on a price to earnings (P/E) ratio of ~31x, this company has a visible roadmap of 15% growth pa over the next few years as acquisition synergies are realised and the benefits of infrastructure exposure, pricing increases and bolt on acquisitions are realised.

Conversely, KFC franchise operator Collins Foods was a poor performer for the portfolio down 6.5% in July. Collins reported their annual result at the end of June which was seemingly well received hitting a high of A\$5.90, before reversing in July to finish at \$5.21. This to us can only be explained by the fact that Collins is not an 'in the club' stock and hence we believe it is only a matter of time before its low valuation (P/E of ~12x) will attract support.

The International portfolio had a reasonable month gaining 2.6% in US\$ as the US quarterly earnings round kicked into gear. It was a roller coast month with the first half seeing strong gains in the US tech sector followed by a reversal after the disappointing Facebook result.

The focus during the month was the quarterly results posted by the US tech component. Google had a standout result earning \$11.45 for the quarter versus market expectations of \$9.75. This number was before a provision for the US\$4.3 billion fine levied by the EU. Clearly continued fines like this may well be a good revenue source for the EU and will probably be copied by other jurisdictions. To put the number in context that fine makes Alphabet as big a contributor to the EU budget as the Netherlands. During the month, Alphabet gained 7.5% and is trading on a forward P/E multiple ex cash of 20x with growth projections just shy of 20% for the next three years.

Netflix disappointed with lower subscriber numbers than expected and having sold half our position pre-result we exited the balance of the holding after the announcement. They are cash flow negative and whilst they have an excellent product this doesn't always equate to an excellent investment. We made good money on Netflix and will look to buy back in should the price decline further from here.

Facebook's result and guidance disappointed the market and the stock fell by 20%. The US\$120bln fall in company value was the largest one day loss recorded in the history of the US stock market, and exceeds the total value of the NZ share market. The Facebook share price move this year is a good illustration of momentum investing going wrong. Despite CEO, Mark Zuckerberg, declaring in early April that fixing data security will significantly impact profitability going forward, Facebook's share price surged over 30% in the Tech rally to all-time highs just prior to the result. We haven't owned Facebook for some time due to teens having a very low adoption rate, but a current valuation of 20x earnings for the power of the Facebook platform can still gain appeal in today's market. Interestingly, even with the result day decline, Facebook's share price is only off ~5% from highs before the Data Scandal story broke in mid-March.

Amazon produced a much better earnings result than forecast on revenues slightly less than the market was expecting. The stock rallied initially very strongly only to give up most of the gains when the tech heavy Nasdaq fell after a disappointing Twitter result. This has been one of our largest positions in the portfolio but for the reasons below we have sold the majority of our position around \$1840. We will own this name again, hopefully at lower prices from here.

The large cap tech stocks have been one of the most crowded trades in the market and whilst we like the businesses as a whole we have been mindful that most are priced with no scope for disappointment. We think the sector may be vulnerable as people come to understand that these businesses are not immune from setbacks as the mixed reporting round showed. We reduced our holdings in a number of the stocks during the month which accounts for the decrease in our overall

equity weightings. Time will tell whether the selloff we have seen develops into a widespread rout but our cautious nature means we prefer to watch from the side-lines. The highly liquid nature of these stocks means moving in and out in size can occur very quickly and with minimal transaction costs.

## TOP 10 HOLDINGS

Mercury	3.8%
Precinct Convertible Notes	2.4%
Metlifecare	2.3%
Contact	2.2%
EBOS	2.1%
Z Energy	1.9%
Cleanaway	1.8%
Sanford	1.8%
a2 Milk	1.7%
Aveo Group	1.6%

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