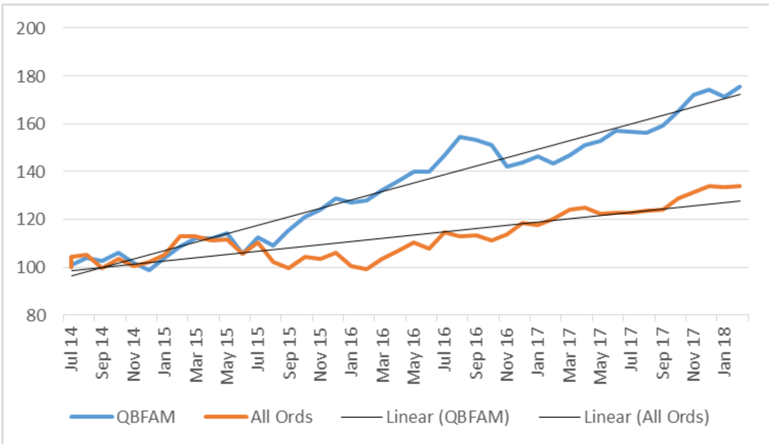
Quick Brown Fox Asset Management

Monthly Report – February 2018

February was one of the stranger months that we have seen in recent times. It began with a rather violent selldown across global markets on the back of rising interest rates. We were well positioned for this selloff, having entered the month with a cash weighting of 38%. The selloff though was short and amazingly the ASX rallied back and finished the month in positive territory, albeit marginally. The portfolio outperformed the market returning 2.6% for the month driven by strong results from AxsessToday (+20.8%), Hansen Technologies (+16.6%) and CSL (+11.4%). Whilst many saw the selloff as an opportunity we believe it may be the first shot across the bow. Globally, interest rates are going up albeit it at a very slow pace. The days of assets being priced off zero percent interest rates are gone. This means that all asset classes (stocks, property, and bonds) will come under pressure and long term buy and hold returns from this point will be poor. Investors need to be selective with their asset purchases and should instead focus on cheap assets with meaningful catalysts. We have increasingly rotated our portfolio away from expensive quality companies to both cheaper companies with growth catalysts and a reasonable holding of cash.

	1 month	3 months	6 months	1 year	2 year (annualised)	Since Inception (annualised)
						1-Jul-14
QBFAM	2.6%	2.2%	12.4%	22.4%	17.1%	16.6%
All Ords	0.2%	1.9%	8.1%	10.8%	16.0%	8.1%
Small Ords	0.0%	2.7%	14.6%	20.2%	18.5%	10.5%

Over the longer term, the fund maintains a strong lead over the market.



Note: All returns are pre fees and unaudited. The fund is not currently available for external investment. To access our investment strategy please contact Tamim Asset Management.

Portfolio News

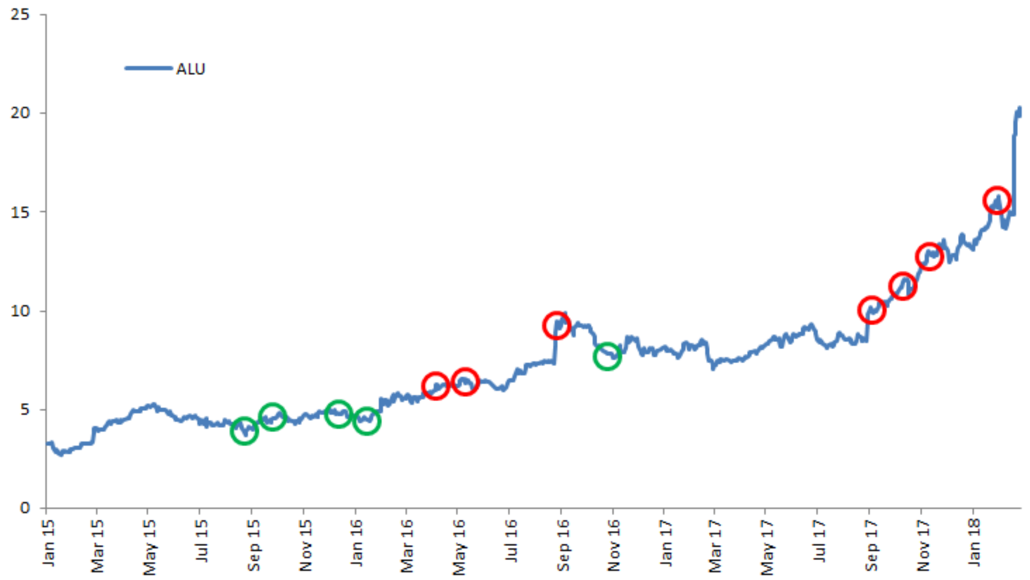
February sees reporting season in Australia with a majority of companies announcing their six month profit or loss to the end of December 31. Overall, reporting season was relatively benign compared to recent years. In fact within the ASX 200, we saw the highest proportion of companies reporting an increase in profit since 2008. Approximately 36% of these top 200 companies that reported earnings exceeded expectations whilst 29% missed. Despite more beats than misses, expectations for earnings growth for the full financial year were revised down from 8.4% to 6.2%. This downgrade to expectations was primarily driven by Commonwealth Bank, Telstra and Rio Tinto.

Some of the things that at the large end of end of town included CSL producing yet another standout result with a very strong turnaround in its vaccines division whilst QBE continued its reputation of being a serial downgrader. Meanwhile Wesfarmers announced a hefty impairment associated with its Bunnings move into the UK, writing down a majority of its original Homebase acquisition.

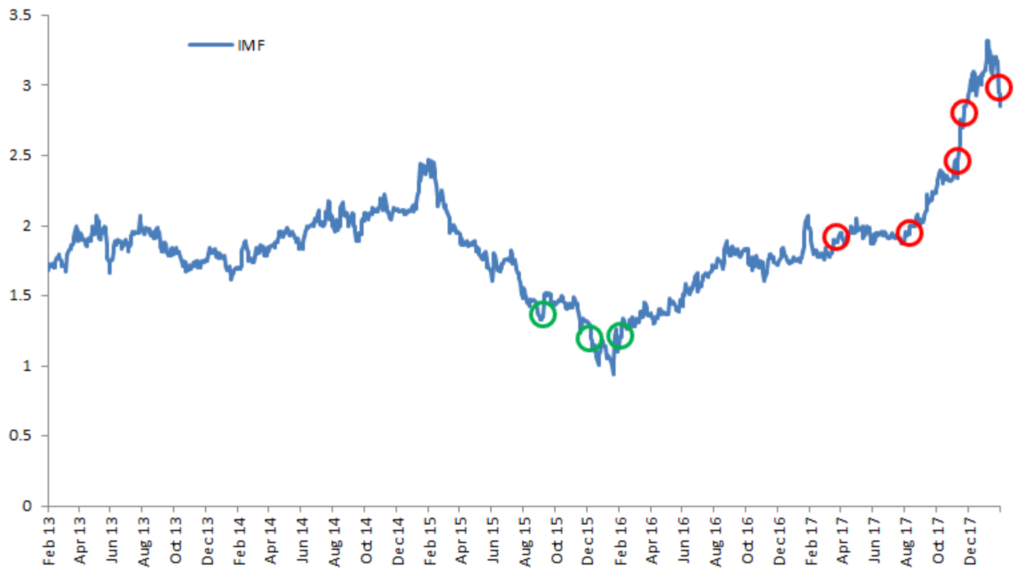
One thing that did surprise us during February was the performance of market darlings on high multiples. Some examples of which are Altium, A2 Milk and Appen. At the time of writing the historical P/E ratios on these companies were 63x, 61x and 71x respectively. On a forward basis, these numbers improve to 42x, 44x and 32x respectively.

Just to be clear, these are three of the highest quality companies listed on the ASX and we have owned all three at various stages in the past. However, the prices of these companies are now such that nothing can go wrong, they are effectively priced for perfection. Also, theoretically these are the companies at most of a derating when interest rates rise, higher multiples mean the shares are of higher duration and hence valuations are more sensitive to changes in the discount rate. Despite this, these stocks continued to surge higher on the back of strong earnings.

Alitum is a company that we owned up until recently. In our opinion, it is the highest quality technology company on the ASX. The below chart shows the share price in recent years, the circles indicate when we transacted (green indicates purchases, red indicates sells). Over the period we held Altium (September 2015 to February 2018) we made an Internal Rate of Return (IRR) of 75.2% including all dividends. This was a very satisfactory investment however post us selling our final parcel at $15.27, the stock has surged another 25%.



During the last month we also exited IMF Bentham. We entered the position back in September 2015. The share price had sold down on the back of two lost cases. At the time the Net Asset Backing (Cash plus investment in cases) was around 90cps, we started buying at around 1.5x assets and topped up the position as it fell. Over the coming few years we saw a rerating of the shares as the company saw multiple case wins and a significant build of its case book.



The company though now is different to when we first entered. The business is in the process of shifting to a capital light funds management model. The shift will mean a business with more consistent profits however the transition over the next few years has the potential to be bumpy. We exited our position and locked in an IRR of 39.5%.

The Portfolio

The fund is currently invested in 21 companies. The cash level is currently 40.0% (up from 38.6%). We added three new small positions which we look to add to over the coming months whilst exiting our positions in Beach Energy, Altium and IMF Bentham. We also trimmed our position in Melbourne IT. We added three new small positions and added to one existing position. Part of the cash balance is committed to a recent capital raising.

GTK	8.5%
AXL	6.2%
HSN	4.5%
DDR	4.0%
CSL	3.9%
Other Positions	32.9%
Cash	40.0%

Sector Positioning

The fund maintains a strong overweight to the IT sector with other exposures in Healthcare, Financials, Industrials, Energy, Consumer Discretionary, Utilities and REITs.