

THB US Micro Cap Fund

Monthly Report – February 2020

Market commentary

The Russell Microcap® Index (Index) returned -3.3% in February.

Health Care (-3.0%) was the best performing sector, followed by Utilities (-5.2%) and Communication Services (-5.2%). Energy (-12.3%) was the worst performing sector followed by Materials (-11.8%) and Consumer Discretionary (-9.2%).

US equities broadly declined as the number of global Coronavirus cases increased, various mitigation steps were put in place and investors priced in uncertainty regarding the overall impact on economic growth and company profits. The divergence between growth and value continued this month as the NYSE FAANG Index was +0.4% for the month versus -8.2% for the broader S&P 500. Similar return divergence was witnessed in Smaller Cap securities as the Russell 2000 Growth was -8.2% compared to -14.6% for the Russell 2000 Value Index.

Prior to the virus spreading, sentiment indicators within the US Economy were strong and improving. While the growing concern regarding the virus will impact the forward readings, the US entered this situation in a strong position. The University of Michigan Consumer Sentiment registered 101 in February which was the second highest reading of the current expansion. Housing remains a strong area within the economy with both permits and starts surging higher. Building permits rose 9.2% to a 1.55M annualised rate which was the highest reading since 2007. A strong labor market and low mortgage rates are fuelling that part of the economy. The US Federal Reserve's will likely lower rates to mitigate the economic impact from Coronavirus. This should further support the strong housing market.

Portfolio commentary

The THB US Micro Cap Fund returned -6.3% in AUD (net of fees) in February underperforming the index by 3.1%.

The portfolio saw positive contribution from stock selection in Energy (+0.3%), Industrials (+0.2%, and underallocation to Financials (+0.1%). Negative contribution came from selection to Health Care (-1.6%), Information Technology (-0.5%) and underallocation in Health Care (-0.3%).

THB's top five performing stocks (from a contribution standpoint) were TPI Composites, Inc. (Industrials, +0.2%), Century Communities, Inc. (Consumer Discretionary, +0.2%), Luminex Corp (Health Care, +0.1%), UFP Technologies, Inc. (Materials, +0.1%) and Renewable Energy Group, Inc. (Energy, +0.0%).

The bottom five performing stocks (from a contribution standpoint) were PAR Technology Corporation (Information Technology, -0.6%), Koppers Holdings, Inc. (Materials, -0.6%), Johnson Outdoors, Inc. (Consumer Discretionary, -0.5%), Addus HomeCare Corporation (Health Care, -0.4%) and LeMaitre Vascular, Inc. (Health Care, -0.4%).

The economic and market impact from the spread of COVID-19 remains a fluid situation, but similar historical occurrences and known facts are useful for navigating through the current market. The many unknowns about the virus typically lead participants to price in worst-

Fund details

Benchmark	Russell Microcap® Index ³
Inception date	5 September 2014
Fund size	A\$247 million

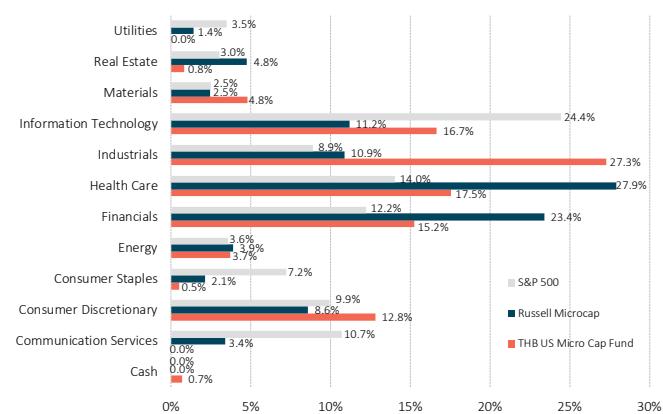
Performance¹ – 28 February 2020

	Fund ²	Russell Microcap®	Difference
1 month	(6.3%)	(3.3%)	(3.1%)
3 months	(6.0%)	(1.5%)	(4.5%)
1 year	(4.1%)	3.0%	(7.1%)
2 years p.a.	5.5%	7.3%	(1.9%)
3 years p.a.	6.4%	8.6%	(2.2%)
Since inception p.a. ²	10.4%	12.0%	(1.5%)

1. Performance figures are presented in AUD on a net, pre-tax basis and assume the reinvestment of distributions. Past performance is not an indicator of future performance. Figures in the table may not sum correctly due to rounding.

2. Fund inception date was 5 September 2014 however inception performance is calculated from 1 October 2014.

Sector allocation⁴



3. The Russell Microcap Index is a capitalisation weighted index of 2,000 stocks that captures the smallest 1,000 companies in the Russell 2000 and 1,000 smaller US based listed stocks.

4. Portfolio holdings and allocations are subject to change and should not be considered as investment recommendations to trade individual securities. The securities identified and described do not represent all of the securities purchased, sold or recommended for client accounts. The reader should not assume that an investment in the securities identified were or will be profitable. There is no assurance that any securities discussed herein will remain in the portfolio at the time you receive this report, or that securities sold have not been repurchased. There can be no assurance that investment objectives will be achieved. A full list showing every holding's contribution to the overall account's performance during the measurement period and calculation methodology is available upon request.

case scenarios, which historically have turned out not to be realised. THB touched on this in its 20th Anniversary letter in 2018 where it detailed the numerous ‘calamities and crises’ that they have managed portfolios through over the years. One more can now be added to the list.

During times like these THB relies on its long history and broad experience to navigate through this challenging period.

As the market situation is fluid, THB is essentially *reflexively* relying on its experience (process, methods, tools, etc.) while making real time decisions based on current information flow, all the time concentrating on risk adjusted returns. And in doing so, THB explicitly acknowledge that you need to accept being wrong in the short term for longer term gains. That is where experience is so important; fighting a behavioural urge to seek safety.

All of the companies THB owns are profitable. They are also well-capitalised, with little to no debt, allowing them to weather (to a very great extent) economic and/or business disruptions caused by COVID-19. Moreover, THB expects them to opportunistically take advantage of dislocations in their share prices via share repurchases and capitalise on weak competitors through acquisitions.

Top 10 holdings

Stock	Sector	Weight
PAR Technology	Technology	2.8%
Renewable Energy Group	Energy	2.5%
Johnson Outdoors	Consumer Disc	2.4%
Century Communities	Consumer Disc	2.1%
Old Second Bancorp	Financials	2.0%
TPI Composites	Industrials	2.0%
Heritage-Crystal Clean	Industrials	2.0%
Addus HomeCare	Health Care	2.0%
Ultra Clean Holdings	Technology	1.9%
Hyster-Yale Materials Handling	Industrials	1.9%

Source: THB Asset Management

Investment strategy

THB Asset Management (THB) is an employee-owned boutique investment management firm based in Connecticut specialising in smaller company strategies. THB's US Micro Cap strategy is based on the belief that there are inefficiencies in the micro cap segment of the market due to lack of analyst coverage, difficulty in identifying value and the impact that management skill has on the direction of smaller companies. THB utilises a disciplined, fundamental bottom-up approach that blends both qualitative and quantitative methods to construct a well-diversified portfolio of companies that possess attractive operating metrics, yet with comparable valuation to the Russell Microcap® Index.

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Asset Management

Portfolio statistics⁵

As at 28 February 2020		
	Fund	Russell Microcap®
Weighted avg market cap	US\$602m	US\$596m
Price/sales	0.7x	0.6x
Price/book	1.6x	1.5x
Dividend yield	0.7%	1.4%
Number of securities	102	1,451
Standard deviation	15.3%	16.8%
Sharpe ratio	0.5	0.5
Beta	0.9	
Tracking error	5.3	
Information ratio	0.04	

5. Portfolio statistics are reported in USD. Source: THB Asset Management

Companies by market capitalisation



Source: THB Asset Management

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