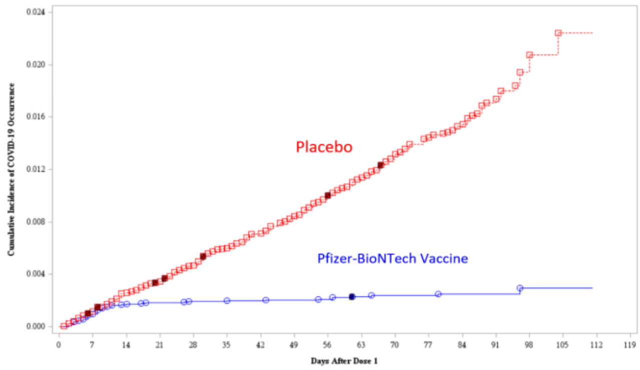
Selector High Conviction Equity Fund

Monthly report – December 2020

Market insights

In our November monthly update, we commented on the progress of two COVID-19 vaccine trials. While there are still considerable challenges in scaling up the vaccine program, the early signs are promising. **Figure 1** shows the cumulative incidence of COVID-19 cases after receiving the Pfizer-BioNTech mRNA vaccine against a placebo. This two-dose vaccine demonstrates strong efficacy, with estimates of over 85% incidence reduction 10 days after the first dose and 95% seven days after a second dose. The global management of COVID-19 via effective vaccination programs may partly define 2021.

Figure 1: Cumulative Incidence of COVID-19 after first dose



Source: Pfizer-BioNTech

Last-minute Brexit concessions on both sides got a deal across the line on 24 December. The trade deal struck by Boris Johnson and Ursula von der Leyen, the European Commission president, is better than no deal, even though it does not cover all of Britain's trade and significant negotiations remain. Financial services, a source of Britain's comparative advantage has not been addressed. Disappointingly, *"passporting"* rights that allow British-based financiers full access to EU customers no longer exist. Digital and data regulation also appears to have been lumped into the *"too hard basket"*.

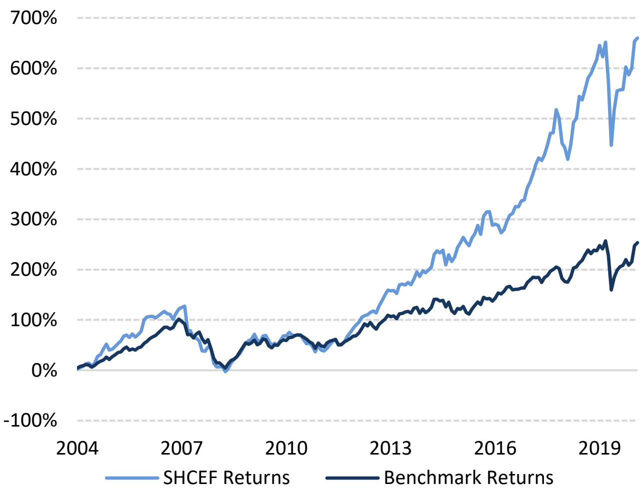
Also, on 24 December, China's State Administration for Market Regulation started an investigation into Ant affiliate, Alibaba Group, for alleged monopoly conduct. On 27 December, the central bank also told Ant to return to its roots as a payments firm, a low-margin, low-risk business along with forcing it to hold significantly more regulatory capital thereby hobbling its growth. This ongoing intervention has little merit but has implications for many. By 28 December, Alibaba had fallen by 13%, or $91bn.

Finally, data from The Economist on debt and capital raisings show the world's non-financial firms raised $3.6t in capital from investors during the year, firmly outpacing new capital raised over the past decade, including the GFC. While cash held by the world's 3,000 most valuable listed non-financial firms has exploded to US$7.6t from US$5.7t last year.

We continue to seek businesses with:

1. Competent management teams
2. Business leadership qualities
3. Strong balance sheets
4. A focus on capital management

Cumulative returns since inception



Inception Date: 30/10/2004
Before fees, costs and tax, and assuming reinvestment of distributions

Top holdings

Company name	Code	Weight (%)
James Hardie Industries	JHX	6.28
Domino's Pizza Enterprises	DMP	5.90
Aristocrat Leisure	ALL	5.07
Reece	REH	4.86
Seek	SEK	4.80
ResMed	RMD	4.65
Altium	ALU	4.41
Carsales.com	CAR	4.36
Nanosonics	NAN	4.23
Iress	IRE	4.15

Unit prices as at 31 December 2020

Entry price	$3.2325
Mid price	$3.2244
Exit price	$3.2163

Performance as at 31 December 2020*

	1 Month	3 Months	6 Months	1 Year	3 Years	5 Years	10 Years	15 Years	Since Inception
Fund (net of fees)	0.70	10.54	14.66	3.42	13.52	13.72	13.66	9.55	11.24
Fund (gross of fees)	0.83	10.63	15.64	5.14	15.70	15.86	15.79	11.57	13.36
All Ords Accumulation Index	1.75	14.43	15.69	3.64	7.44	9.26	7.89	6.87	8.12
Difference (gross of fees)	(0.92)	(3.80)	(0.05)	1.50	8.26	6.60	7.90	4.70	5.24

*Performance figures are historical percentages, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Returns assume the reinvestment of all distributions. For periods greater than one year, returns are annualised. Performance can be volatile and future returns can vary from past returns.

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Portfolio commentary

Appen (APX:ASX)

Appen, a global leader in providing high quality training data for machine learning and artificial intelligence (AI) products, released a trading update this month lowering underlying earnings (EBITDA) guidance for the full year 2020 to $106m-$109m, compared to $125m-$130m provided at the half year results.

Management attributed the decline to exchange rate headwinds and the impact of COVID-19 on new business development, renewals with smaller customers and importantly, the lack of the usual last quarter calendar year demand ramp up from major customers. The trading update is undeniably disappointing and highlights both the lack of visibility Appen has on future orders, as well as the risk associated in having such a concentrated customer base.

Management are focused on matters within their control, which is to maintain the delivery of high-quality data at speed for customers. Appen operates as a leader within its space and following the 2019 acquisition of Figure Eight's technology platform, now have a bundled software and services solution to offer in a market that is expected to deliver growth north of 20% annually. Financially, Appen has a capital light balance sheet and the ability to self-fund its growth initiatives for the foreseeable future.

Appen has a market capitalisation of $3.0b and recorded a net cash position of $92m at June 2020.

IOOF Holdings (IFL:ASX)

The competition watchdog, the ACCC, has announced that it will not oppose IOOF's proposed acquisition of MLC. Post the transaction, IOOF will be the foremost advice-led wealth manager with circa $510b of funds under management, advice and administration (FUMA). While this is a significant step in continuing to build scale, the announcement was shortly followed by IOOF's decision to terminate its platform relationship with BT.

Ending this relationship, with associated FUMA of $18.8B, results in annual revenue and profit falling by $26m pre-tax. IOOF were left with few choices here, believing that these revenues were threatened by the potential of lower pricing at BT's discretion. Further a customer transition, subject to high attrition, was deemed expensive and unattractive. Importantly, IOOF will receive a one-off settlement of $62m pre-tax in recognition of their rights under the agreement.

To align with partners that fit the company's open architecture approach, IOOF has entered into a platform agreement with HUB24. Under this agreement, HUB24 will act as the platform administrator and custody provider in addition to developing private label super and investment products with IOOF. Here IOOF controls the client relationship. Over time, financial planners may transfer clients over to HUB24 or IOOF's proprietary Evolve platform, subject to the best interest test. However, this will undoubtedly take time.

CEO Renato Mota noted, *"The decision to change the provider relationship now provides us with long-term certainty as we focus on the effective implementation of our new platform strategy and growing returns for shareholders. It is important we work with partners who fit with our open architecture philosophy. Enabling choice is a key feature of our strategy".*

IOOF has a current market capitalisation of $2.3b.

Performance contributors

Top five	Contribution (%)
Domino's Pizza Enterprises	0.86
Nanosonics	0.72
Reece	0.43
Seek	0.42
PolyNovo	0.38
Bottom five	**Contribution (%)**
Cochlear	(0.69)
TechnologyOne	(0.39)
Flight Centre Travel Group	(0.21)
Appen	(0.20)
James Hardie Industries	(0.20)

Industry exposure

Industry group	Weight (%)
Software & Services	24.04
Consumer Services	17.70
Health Care Equipment & Services	16.30
Media & Entertainment	10.64
Capital Goods	7.81
Materials	6.28
Diversified Financials	4.74
Pharmaceuticals, Biotech & Life Sciences	3.97
Insurance	2.50
Household & Personal Products	2.41
Automobiles & Components	1.94
Consumer Durables & Apparel	1.38
Cash & Other	0.29

About Selector

Selector Funds Management ("Selector") specialises in high conviction, index agnostic, concentrated portfolio management (AFSL 225316). The investment team have a high level of experience, are owners of the business and invest in the funds alongside clients. Selector has a long-term track record of performance.

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