TMS High Conviction Portfolio

Model Portfolio Profile

A Professionally Managed Portfolio of Australian Shares

The TMS Capital High Conviction portfolio is a separately managed account, or SMA, actively managed by TMS Capital Pty Ltd. A Managed Account is a personalised investment portfolio run like a traditional managed fund by professional managers. However, unlike a traditional managed fund or unit trust the investments/shares are beneficially owned by the individual investor(s).

About the Manager

TMS Capital is a boutique investment management business providing unique, direct investment solutions to the private client market.

TMS specialises in the active management of diversified investment portfolios for retail investors, with an emphasis on listed Australian shares and securities.

Model Objective

The objective of the TMS High Conviction portfolio is to provide investors with long-term capital growth and tax effective income. The portfolio aims to deliver a total return performance in excess of the All Ords accumulation index over rolling 5 year periods.

Value Investment Philosophy

The manager's objective is to generate excess returns over the All Ords Accumulation index. We aim to achieve this by investing in a portfolio of businesses that is truly index unaware, ignores tracking short term performance and has a genuine focus on backing those companies whose profit growth we believe will outstrip the market.

Given a sufficient period of time the market should be efficient at rewarding those businesses of a higher quality than the average.

We seek to invest in those companies we believe have a high probability of significantly increasing earnings per share over a 5 year period. Experience tells us that over such a timeframe total shareholder returns will track profit trajectory.

Our goal is to find those businesses with proven management teams; high returns on capital employed, strong balance sheets operating in industries we feel have structural tailwinds. Our belief is that adopting a buy and hold mentality when investing in stocks offering these attributes will result in superior performance over attempting to trade them.

Key Portfolio Features	
Model Inception	1 July 2015
Benchmark	S&P/ASX All Ords Accumulation Index
Number of stocks	15-25
Cash Allocation	0-50%
Investment Horizon	At least 5 years

Key Portfolio Features	
Authorised Investments	All companies listed on the ASX.

Portfolio Structure

Top 10 Holdings (alphabetical order)

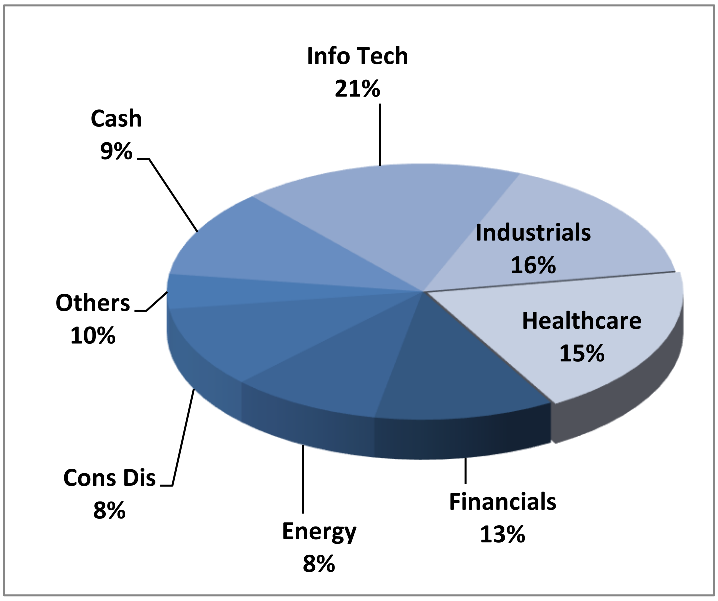
ASX Code	Company Name
ALL	ARISTOCRAT LEISURE
ALU	ALTIUM LIMITED
APX	APPEN LIMITED
CSL	CSL LIMITED
FPH	FISHER & PAYKEL HEALTHCARE
MQG	MACQUARIE GROUP LIMITED
RMD	RESMED INCORPORATED
SEK	SEEK LIMITED
WTC	WISETECH GLOBAL
XRO	XERO LIMITED

Performance and Sector Allocation

Return %	3m	1yr	3yr p.a	Since Incep. p.a
TMS High Conviction	**-20.3**	**-4.7**	**+12.0**	**9.4**
All Ords Accum Index	-23.9	-15.0	-0.7	3.4
Outperformance	**+3.6**	**+10.3**	**+12.7**	**+6.0**

Past performance is not indicative of future performance.

Market Commentary



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The March quarter of 2020 saw one of the most extraordinary moves ever witnessed on the local share market. After a very strong January the market moved from ignoring Corona, to seeing it as a China based issue to causing the most severe sell-off we've seen in the ASX's history. The market fell 41% in just 23 days, to put this into perspective it took one year and one week to deliver a similar return through the GFC. Our portfolio finished the quarter outperforming the broader market by 3.6%, a result we'd normally be very happy with, however a 20% fall in a quarter was extremely painful to experience.

We and our families are heavily invested in the fund and our interests are completely aligned with our investors. Although this has been the toughest period in the fund's history, we remain convinced our businesses represent a very different investment proposition to the overall market and are working harder than ever to position the portfolio in a rapidly evolving outlook.

The issues surrounding Covid-19 are completely unprecedented. It is no exaggeration to say that the events we are witnessing from an economic, health and market viewpoint have never been seen by anyone on this planet, there is no playbook to look back at and get some sense as to what the future holds.

Governments have literally been forced to effectively engineer a deep recession to give their citizens the best possible health outcomes in combatting the virus. This is being done with varying degrees of success in different countries, but the real test will be how the virus behaves as economies are slowly opened back up. Simultaneously we have seen central banks, government, regulators and the banks provide very rapid, coordinated and extraordinary size of stimulus to get the economy through the period but there is only so much more that can be done.

There are no answers to the big question's investors all face. How long this lasts for, how severe the financial consequences of fighting the virus turn out to be will only be known in hindsight. The best we can do is continue to take a long-term view on the businesses held across our portfolio.

Australia has acted decisively, with total combined stimulus of $300bn due to hit the economy and markets over the next twelve months. This has done a lot in helping calm the markets for now and seeing more rational pricing emerge. Incredible decisions by government are similarly leading to incredible movements in all asset markets.

In this environment its important to focus on the principles that have served us well to date and not to get to focussed on the dramatic daily moves we've seen through the quarter. Some businesses of course will take an earnings hit as a result of the environment they face but it's important to look beyond this time toward where earnings will revert. We will continue to hold businesses we believe:

- Can meaningfully grow earnings over the longer term without the help of an economic tailwind.
- Have invested management teams who oversee a strong company culture.
- Possess attractive financial metrics, ideally reinvesting capital at high incremental rates of return.
- Have the liquidity to survive the shutdown of the global economy.

Over the last month our primary focus has been on analysing companies balance sheets and their ability to withstand a cash crunch to their business. Solvency is the principal initial concern and it has helped that many of our businesses came into this downturn with either net cash or a very conservatively geared balance sheet. This doesn't necessarily mean a company will avoid shoring up the balance sheet through a raising, different boards will take different views on how long this environment could last for. It should however mean that there is less dilution across our portfolio than the recapitalisation we could see across the broader market.

Post March 30 further cash has been raised following a strong recovery in the value of the portfolio giving us the ability to take advantage of any raisings our companies decide to proceed with.

Portfolio Performance

Virtually all holdings in the portfolio were sold off through the quarter although amazingly three companies actually rose in price. These were CSL, Resmed and Fisher & Paykel Healthcare, 22% of the portfolio is invested in these three businesses and is the main reason for the overall outperformance. All three have been held since inception.

Fisher & Paykel has experienced an unexpected tailwind, it is one of the worlds largest manufacturers of ventilators which of course now are highly sort after. Resmed has begun refashioning its sleeping masks into ventilators which will likely see a sugar hit to earnings although this will likely offset weakness in the core sleep business, doctors currently have bigger priorities than sleep testing patients. Finally, CSL, the largest player globally in flu, is likely to see massive demand for its flu shots this year and will likely be involved in the manufacture and distribution of any Covid-19 vaccine. Plasma is also being trialled to help treat Corona patients but the company has advised it is getting tougher to source blood due to self-distancing.

The worst three performers were Aristocrat (closure of casinos, pubs and clubs globally), Wisetech (seizure of global trade) and Sydney Airports (effective closure of Australia's boarders).

We continue to stick with these businesses, on a more normalised earnings base the valuations appear highly attractive.

As at March 30 the funds cash position was close to 7%. The ability of a manager to rapidly skim and add to positions through short term volatility is a key advantage we believe the SMA possesses.

Portfolio Commentary

The March quarter includes the February earnings season which now seems a very distant and by now largely irrelevant flurry of news. Generally, though we were pleased with the updates of our stocks.

Nearly all companies met or bettered expectations with outlook statements broadly positive in nature.

Three companies trimmed guidance for the year, WiseTech and Altium who both reported issues as a result of the closure occurring across China. Interestingly Altium has since reported a reacceleration of its business in the country but is of course now facing uncertainty as the rest of the world deals with the Virus. Link Market Services downgraded due to the issues they faced around Brexit. The PEXA business performed very strongly and we think could see an acceleration of take-up in a self-distancing world.

Challenger, CSL, Reece, A2 Milk and Afterpay all reported stronger than expected results.

Since the earnings season finished in February virtually every company across the market has withdrawn guidance. Speaking to a number of management teams the feedback is that many companies have absolutely no idea where their final number will land for the year.

Activity in the portfolio was fairly muted through the quarter. We took some advantage of volatility in individual share prices that you typically do see around results / earnings guidance. We trimmed our holding in Challenger and Mineral Resources during the Feb reporting season whilst adding to Sydney Airport, Auckland Airport, WiseTech and Altium during the vicious selloff the companies experienced in March. This is an approach we have typically taken since the fund's inception; we consider all these companies as core holdings but have been happy to let some go into extreme strength and back into weakness.

We bought into one new business during the quarter, Tyro Payments. Tyro was a new entrant to the ASX floating onto the exchange late last year. The company has developed a highly competitive payments solution used principally by the hospitality and healthcare industries but really is morphing into a neo bank, using leading tech to encroach on the Big Four banks. It has an impressive register of shareholders and although of course very much at the forefront of the lockdown

Looking Forward

We are experiencing an unprecedented time and it is not clear where markets will head from here. Valuations appear highly attractive if compared to where we believe earnings can normalise to.

In a period of waning economic growth, it's more important than ever to find those stocks that can grow their profits without relying on a growing economy and looking to our portfolio we are confident in its future. Our collection of companies will grow their earnings significantly faster than the overall market in FY 2020 and beyond. They have some of the most impressive CEO's in the country at the helm looking to leverage opportunities with much stronger balance sheets than the overall market.

This is more important than ever. Sticking with these businesses is the key to long term investing success.

$500,000 invested in the fund at inception – 1 July 2015 was worth $681,635 as at March 30, 2020.