ASX LISTED INVESTMENT COMPANY (TICKER: CLF)

MONTHLY INVESTMENT REPORT: DECEMBER 2019

Fund Description

Concentrated Leaders Fund Limited (CLF) is a concentrated portfolio of leading Australian companies. The CLF investment team uses a top-down macro thematic, quantitative filters and bottom-up fundamental research.

Fund Objective

CLF is a geared listed investment company, which invests primarily in companies within the S&P/ASX 200 Accumulation index. CLF is focused on providing investors with capital growth and a consistent yield.

Net Tangible Assets (NTA) as at 31 December

Total Investments	**$112,046,219**
NTA	**$81,319,218**
Shares on Issue	**59,401,514**
NTA per Share (pre-tax) *	**$1.37**
NTA per Share (post-tax) *	**$1.31**
Share Price	**$1.32**
(Discount)/Premium to NTA (pre-tax)	**(3.65)%**
(Discount)/Premium to NTA (post-tax)	**0.76%**
Fully Franked Dividend Yield	**10.01%**

* On realised and unrealised gains.

Fund Information

ASX Code	CLF
Date of launch	September 1987
Benchmark	S&P/ASX 200 TR Index

Service Providers

Custodian	National Australia Bank
Administrator	Fundhost Limited
Banker	National Australia Bank
Auditor	Deloitte Touche Tohmatsu
Legal Advisor	Watson Mangioni Lawyers

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Portfolio and Market Review

Investment Performance

Performance as at 31/12/2019 **	1 Month	3 Months	6 Months	12 Months	Financial YTD	Since Inception *
CLF	-0.67%	3.53%	4.64%	20.34%	4.64%	18.77%
Benchmark	-2.17%	0.68%	3.06%	23.40%	3.06%	19.89%
Value Add	1.50%	2.85%	1.58%	-3.06%	1.58%	-1.12%

* Inception date reflects when management of the fund was internalized as of 1 January 2018
** Gross performance excludes all expenses, fees and taxes. Net performance is reflected in the NTA calculations.

The portfolio returned -0.67% on a gross basis (pre-fees and taxes) in December versus the benchmark return of -2.17%. This equates to a 2.14% decrease in pre-tax NTA and a 2.24% decrease in the post-tax NTA.

For the financial year to date, the portfolio has delivered a return of +4.64% on a gross basis versus the benchmark's +3.06%. This represents a relative performance of +1.58%.

Market Review

The S&P/ASX 200 Total Return Index significantly underperformed the rest of the world in December, with the MSCI All Country World Index gaining 3.39% and the S&P 500 Index gaining 2.86% (both in USD terms).

For the calendar year, Australian equities returned +23.40%, which was the strongest annual performance since 2009. While this was a stellar performance primarily on the back of lower interest rates it was marginally weaker than global equities, which returned +24.38%. The S&P 500 Index returned 29.23% for the year, with technology stocks leading the way. The Nasdaq Composite Index gained 35.59% for the calendar year.

Global equity markets fell early in the month after US President Trump increased tariff rhetoric by suggesting that South America and Europe could increasingly become targets for increased tariffs – this included potentially 100% tariffs on French goods. He also reiterated that the US would increase tariffs on China if no deal was reached prior to the mid-December deadline. However, subsequent positive US-China trade news and a strong US jobs report, saw most global equity markets rebound strongly by the end of the year.

In Australia, yields increased over the month with 10-year yields increasing from 1.00% to 1.32% as a result of the improved trade environment and global economic data. These factors also saw the Australian dollar rally by 3.81% to close the year at US $0.7021. These were some of the largest monthly moves this year for both markets and weighed heavily on the domestic market.

In terms of domestic sector performance, the primary movers were:

1. Consumer Staples (-8.1%) was the worst performing sector with WOW (-9.1%) and COL (-8.7%) after Woolworths admitted not paying salaried staff appropriately.
2. Telecommunications Services (-7.8%) also performed poorly with TLS (-8.3%) giving back strong gains from last month as bushfires affected several services.
3. Materials (+1.5%) was the only sector to deliver a gain for the month.

Portfolio Review

The portfolio outperformed during the month by +1.50%.

December's result was very pleasing and delivered our third straight month of outperformance such that, for the quarter, the portfolio outperformed the S&P/ASX 200 Total Return Index by 2.85%. This was despite the benchmark delivering a positive return and CLF continuing to hold ~25% in cash.

Our underweight exposure to financials added to returns with all the major banks ending the month weaker. We continue to see elevated risks for the sector and maintain this underweight position; albeit that WBC, ANZ and NAB have all become more attractively priced. CBA has held up spectacularly well with investors seemingly rotating into it given its regulatory issues are arguably better known than its competitors and it has more exposure to the improving domestic housing market.

Major Contributors:

NST (+17.9%) – Rallied strongly after raising $765 million in fresh capital to fund its US$800 million purchase of Newmont Goldcorp's share in Kalgoorlie Consolidated Gold Mines. The transaction is expected to be earnings accretive and delivers Northern Star a half-share of one of the most significant gold systems in the world (other half is owned by Saracen Mineral Holdings).

BVS (+4.84%) – Continued to rally following its AGM in November, when its CEO confirmed that it was on target to deliver its target profit growth. The UK election also provided a positive stimulus for Bravura with Boris Johnson's victory benefitting most stocks with UK exposure.

WEB (+3.7%) – Webjet rose strongly on speculation that it was being shopped around to private equity firms by a major investment bank and hence could be a takeover target.

Major Detractor:

SIQ (-21.15%) – Fell sharply after announcing that changes to the product terms at its add-on insurance underwriter would reduce net profits by ~$4 million. This represents a 10% downgrade based on its FY19 earnings guidance. Thankfully, this is only a very small position in the portfolio.

TWE (-13.16%) – Treasury Estate gave back all of November's gains plus some after the Beijing High Court overturned an earlier decision against a copycat winery over similar branding with regards to protecting its highly valuable 'Penfolds' brand.

TNE (-9.8%) – Fell sharply on no specific news, however it did rally 24.7% the prior month so it is likely, and understandable, that some investors took some profits off the table.

Sector Exposure

Sector	Weight (%)
Consumer Discretionary	8.3%
Consumer Staples	5.2%
Energy	1.5%
Financials	16.5%
Health Care	6.4%
Industrials	11.7%
Information Technology	6.4%
Materials	10.9%
Real Estate	6.5%
Telecommunication Services	0.0%
Utilities	2.9%
CASH/LIQUIDITY	**23.6%**

Top 10 Holdings in alphabetical order

Code	Company Name	Sector
ALX	ATLAS ARTERIA LTD	Industrials
AMC	AMCOR LIMITED	Materials
APA	APA GROUP	Utilities
BHP	BHP BILLITON LIMITED	Materials
CBA	COMMONWEALTH BANK OF AUSTRALIA	Financials
CSL	CSL LIMITED	Health Care
MQG	MACQUARIE GROUP LTD	Financials
NXT	NEXTDC LIMITED	Information
TCL	TRANSURBAN GROUP	Industrials
WEB	WEBJET LIMITED	Consumer

Outlook

There are several key factors that we are considering when assessing the market, positioning the portfolio and selecting securities. These include:

1. Valuation – The aggregate market is trading at 17.7x next year's earnings, which is easily the highest multiple in recent memory. The historical peak for Australian equities has been ~16.5x but record low interest rates have significantly impacted what investors are willing to pay for both earnings growth and yield. Both Australian and global markets suggest that these higher valuations are warranted and that easy monetary policy rules all other factors, but we are a little more skeptical and think that monetary policy is nearing the end of its effective influence and that other risks are not being appropriately priced.
2. Corporate fundamentals – Earnings growth expectations have weakened considerably over the past 12 months and there is little to suggest in aggregate these will improve. However, there are specific industrial companies which are demonstrating sustainable above-market earnings growth and identifying these is our primary goal. We continue to see opportunities in offshore earners despite the slumping global economy and we continue to favor the technology and industrials sector despite some lofty valuations. We are however being selective and prudent with our entry timing.
3. Economic fundamentals – the Australian economy is weaker than what the headline numbers suggest with public spending and net exports providing the bulk of GDP growth. The private sector is bordering on recession and if considered on a per-capita basis, is likely already there. We think that companies focused purely on the domestic economy and consumers will continue to face headwinds. As such, we are primarily focused on businesses which are exposed to the global consumer and/or domestic infrastructure or public spending.
4. Offshore Influences – The easing of trade tensions has been a major positive for global markets recently and with a phase-one deal expected to be signed in mid-January, this can only be a positive. Likewise, inflation is expected to remain low and this will allow central banks to continue with their ultra-easy monetary policy stances. As such, the environment which drove equities higher in 2019 is likely to continue in 2020, unless geopolitical risk increases and/or inflation surprises to the upside. US/Iranian tensions have increased significantly recently and the near-term path of markets will largely be determined by how each party reacts in the coming weeks/months. If the situation escalates there is potential for it to impact oil prices, inflation, consumer confidence and trade negotiations if China and/or France react negatively to US actions.

Overall, however we remain positive on the Australian equity market given the low interest rate environment, but would like valuations to moderate somewhat to provide additional investment opportunities.

The team at CLF wish you and your family a fantastic 2020.

Important Information

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