

SEC Results 1HFY2020

Highlights

1HFY20 profit	Company Performance ¹	Interim dividend	Yield
\$4.6m	+4.7%	3.0c	3.9% ²

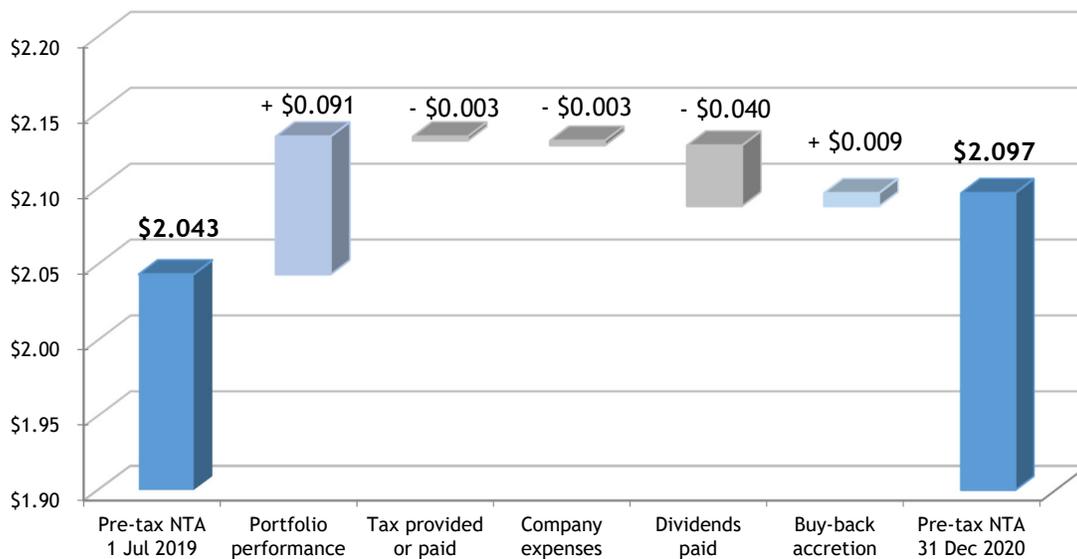
- 1H2020 net profit after tax of \$4.6m
- Interim dividend of 3.0 cents per share (fully franked), an increase of 50% on prior corresponding period
- Company NTA performance of +4.7%
- Portfolio performance +4.5%
- On-market share buy-back continues
- Company well poised to act as consolidator and/or raise additional capital to improve scale

Spheria Emerging Companies Limited (ASX:SEC or the Company) recorded an operating profit of \$4.6m for the half-year ended 31 December 2019 (1HFY20).

Company NTA performance, which includes the impact of tax on realised gains and other earnings of the portfolio, was +4.7% for the half-year when adjusted for dividends paid.

The Company's investment portfolio performance was +4.5%, exceeding its benchmark by 0.6%.

NTA performance breakdown for 1HFY20



¹ Calculated as movement in Company's pre-tax NTA, which includes tax on realised gains/losses and other earnings, but excludes any provision for tax on unrealised gains/losses, adjusted for dividends paid by the Company.

² Annualised dividend yield when combined with FY19 final dividend of 4.0 cents per share, calculated on share price as at 31 December 2019 of \$1.79

Interim dividend

The Board has resolved to pay a fully franked interim dividend of 3.0 cents per share, which is a 50% increase on the previous half-year. The dividend will be paid to SEC shareholders on 20 March 2020 with a record date of 6 March 2020. When combined with the final FY19 dividend of 4.0 cents per share paid in September 2019, this equates to an annualised dividend yield of 3.9%² or a grossed-up yield including franking of 5.6%². The Company's intention is to pay a dividend to shareholders at least annually, subject to available profits, cash flow and franking credits.

Dividend ex-date	Record date	Payment date
5 March 2020	6 March 2020	20 March 2020

Discount to NTA

At 14 February 2020³, SEC shares were trading at a 14.6%⁴ discount to pre-tax NTA (\$2.089 per share). The Board acknowledges this unsatisfactory position and remains committed to addressing the discount to NTA. It is noted however, that SEC is not in a unique position and the majority of small cap equity LICs are currently trading at similar discounts to SEC.

The Board considers the Company as well positioned in the Australian small cap LIC sector. Spheria Asset Management Pty Limited (the Manager) is a high-quality active manager with a proven track record of outperformance in Australian small cap companies. SEC is one of only four ASX listed LICs focusing on small companies that has a market capitalisation in excess of \$100 million⁵. The Board wishes to use this position to attain additional scale (regarded as assets greater than \$200 million) in order to improve SEC's liquidity, lower operating costs, broaden research coverage and improve shareholder diversification. To achieve this, the Board will look for consolidation opportunities to acquire other small cap LICs and/or raise additional capital to achieve scale, should it be deemed in the best interest of shareholders.

In addition, the Company continues to focus on shareholder engagement together with the on-market share buy-back that continues as one of the Company's capital management initiatives, as outlined in greater detail below, in addition to its dividend policy.

On-market share buy-back

On 24 June 2019, the Board announced that the Company had decided to implement an on-market buy-back of the Company shares as a proactive measure to address the share price of the Company trading at a persistent discount to the NTA of the Company.

The Company committed to purchase up to \$5 million worth of shares during the 12-month period commencing 1 July 2019 and ending 30 June 2020, at the prevailing share price where the discount to the last disclosed NTA is in excess of 10%.

³ Date of last published NTA backing

⁴ Share price at 14 February 2020 of \$1.785

⁵ Source: ASX Investment Products Australia Small/Mid cap January 2020

As at 25 February 2020, 2.4m shares had been acquired valued at \$4.2m. The buyback has been accretive to the Company's NTA as the shares are acquired at a discount, adding approximately \$0.01 per share to the NTA.

Investment by the Manager

As at 31 December 2019, the aggregate holding of shares in SEC of the Manager and executives of the Manager (who are not acting in concert with each other) was in excess of 750,000 as the Manager continues to acquire shares in the Company. The Manager is committed to being a long term investor in the Company.

Shareholder webinar on results and portfolio

The Board invites you to the upcoming shareholder webinar on 9th March 2020 at 10.30am (Sydney time EADT). The webinar will provide an update on the Company's investment portfolio by Matthew Booker and Marcus Burns, the portfolio managers of Spheria Asset Management Pty Ltd.

Shareholders are invited to register at the following link:

https://pinnacleinvestment.zoom.us/webinar/register/WN_XpcSUEQqS3mQmnrCN5_mGw

Calvin Kwok
Company Secretary
26 February 2020

Additional shareholder information

Performance as at 31 December 2019

	Since 1 July 2019	Since inception p.a.
Company*	4.7%	4.7%
Portfolio**	4.5%	6.7%
Benchmark***	3.9%	6.5%
Portfolio Outperformance	+0.6%	+0.2%

*Calculated as movement in Company's pre-tax NTA, which includes tax on realised gains/losses and other earnings, but excludes any provisions for tax on unrealised gains/losses, adjusted for dividends paid by the Company.

**Shows how the portfolio, for which the Manager is responsible, has performed after deducting management fees, costs and taxes and performance fees (if applicable).

*** S&P/ASX Small Ordinaries Accumulation Index.

Manager's commentary

Portfolio performance

The investment portfolio increased 4.5% for the six-month period ending 31st December 2019, outperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.6%. In the December quarter, the Federal Reserve increased the size of its balance sheet to counter short term funding spikes in the US repo market, this alleviated stress in the interbank lending market but also fed asset price strength particularly in global share markets. The portfolio benefitted from this and a mild rotation away from growth to value. The three largest contributors to portfolio performance during the half year were Class (CL1), City Chic Collective (CCX) and GBST Holdings (GBT), while the three largest detractors that we owned were Seven West Media (SWM), A2B Australia (A2B), and Bega Cheese (BGA).

Market outlook

We believe the market has become extremely inefficient in recent years due to synchronised central bank stimulus and the rise of passive and quantitative strategies which generally lack any valuation anchor. This has led to pockets of extreme under and over valuation, which we as active managers have endeavoured to exploit. The problem being it has been a one-way path in recent years with the expensive simply getting ever more expensive and the inexpensive becoming even cheaper. The truth probably lies somewhere in between for the market and the catalyst for a rotation (unfortunately) may be central banks eventually ending their money printing experiment. The impact of such a move could be catastrophic for companies that have relied on cheap capital and have no defined path to profitability or have valuations that will never be supported by the profitability ultimately required. We think it safer to own companies that generate solid cash flows, have competitive advantage and are not reliant on third party funding to survive. Incredibly, many of these companies are out of fashion and therefore the risk-reward equation appears heavily skewed, in our favour.

About Spheria Asset Management Pty Limited (Manager)

Spheria Asset Management Pty Ltd is a fundamental-based investment management firm with a bottom-up focus, specialising in small- and micro-cap companies, which can provide higher returns in the long term than their larger peers.

The Manager is majority owned by its team with nearly 100 years of combined investment experience. The Manager's performance culture is underpinned by sensible incentives, a focused offering and the outsourcing of non-investment functions to minority partner Pinnacle Investment Management Limited.

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