Quarterly Update

30 June 2022

Intelligent Investor Australian Equity Income Fund (Managed Fund) (ASX:INIF)

Issued by
InvestSMART Funds Management Limited
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Managed by
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ACN 109 360 983
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ASX Code: INIF

"When I first started out, I did thorough papers covering every aspect of a stock or industry. Before I could make the presentation to the stock selection committee, I first had to submit the paper to the research director. I particularly remember the time I gave him my paper on the banking industry. I felt very proud of my work. However, he read through it and said, "This is useless. What makes the stock go up and down?" That comment acted as a spur. Thereafter, I focused my analysis on seeking to identify the factors that were strongly correlated to a stock's price movement as opposed to looking at all the fundamentals. Frankly, even today, many analysts still don't know what makes their particular stock go up or down."

— Stan Druckenmiller

The Fund increased 4.4% for the year comparing favourably with the market's 6.5% loss. The fund added 3% of outperformance in the final quarter following the market's 12% fall.

It's been one of the worst starts to a year for the stockmarket, yet valuations remain high for quality businesses. There is plenty of value in our largest holdings, though, particularly those still suffering from COVID shutdowns, such as **Star Entertainment**, **LendLease**, **Tabcorp**, **Auckland Airport** and **RPM Global**.

Performance (after fees)

	3 mths	1 yr	2 yrs (p.a)	3 yrs (p.a)	S.I. (p.a)
II Australian Equity Income Fund	–8.7%	4.4%	20.1%	8.6%	6.1%
S&P ASX 200 Accumulation Index	–11.9%	–6.5%	9.3%	3.3%	5.7%
Excess to Benchmark	3.2%	10.9%	10.8%	5.3%	0.4%

Inception (S.I.): 18 Jun 2018

Fund overview

The Intelligent Investor Australian Equity Income Fund (ASX:INIF) is a concentrated portfolio of 10-35 Australian listed stocks. The Fund focuses on large, mature businesses with entrenched competitive advantages, and dominant smaller companies we believe will produce strong cash flows to support dividends in the future.

5+ yrs
Suggested investment timeframe

10 - 35
Indicative number of securities

Risk profile: High
Expected loss in 4 to 6 years out of every 20 years

S&P/ASX 200 Accumulation Index
Benchmark

Investment fee
0.97% p.a.

Performance fee
Nil

Dividends from these stocks will recover in the years ahead and restore the yield of the fund to normal levels. Yield aside, we're pleased that the fund has performed so well since we started managing money back in 2015. Particularly given how hard it was to match insanely priced growth stocks toward the end of one of the biggest asset bubbles ever, if not the biggest.

We've also been underweight iron ore stocks that are still enjoying high iron ore prices partly due to Brazilian miner Vale's ongoing issues. But, as with the banks, the last of which we sold some time ago, we don't expect high capital gains from these major dividend paying sectors over the next decade and dividends may be cut severely.

Amazingly, most bank share prices are near or below where they were in 2011, despite an extraordinary house price boom. Now they're facing more competition and higher costs.

The banks have shown what happens to your dividends and returns when you can't grow your earnings. That's why we focus on companies that can grow their earnings and dividends rather than buying stocks that pay the highest yields today.

Success during a bear market is not just about outperforming the market, though we obviously prefer it like you. But rather setting the fund up for the next bull market with as many of the best businesses we can add at good prices.

It's these businesses that will increase their earnings the fastest and compound your money the quickest. All while paying a growing and increasingly valuable stream of dividends in what could still be a low interest rate environment given the world's enormous debt levels.

Without pricing power no company can increase its earnings consistently over long periods. And without growing earnings you can't increase dividends for long before hollowing out your business leading to mediocrity and failure.

We're delighted valuations are falling and can't wait to see what the fund looks like at the same time next year.

Portfolio

BHP completed its demerger of its oil and gas business bought by **Woodside**, so we ended the quarter with a little less BHP and a little more Woodside in the portfolio.

Ditto for **Tabcorp**, which split its wagering and lottery businesses. We retained our holding in **The Lottery Corporation**, which was most of the value, and then increased our stake in Tabcorp. It's trading well below previous takeover offer prices for both Tabcorp and a similar rival that was eventually acquired, as the industry consolidates.

Tabcorp CEO Adam Rytenskild has recently received some favourable regulatory news that helps level the playing field with his digital rivals. He'll have his plate full this year with the bid for Western Australia's wagering license, most likely a takeover offer or two and lastly with operations getting back to normal post COVID.

We don't need a takeover to do well from here. Provided Tabcorp's earnings get back to normal, the stock should trade at a materially higher price, particularly as dividends are restored.

Credit Corp's share price sank after it announced benign credit conditions will slow growth next year, particularly in Australia. Higher interest rates should change that, which is why we topped up our position.

In February, Credit Corp purchased a small book of NZ ledgers from smaller rival **Collection House**, which is now in administration. Credit Corp should be able to pick up some cheap assets in the process, which is a timely reminder of why you should generally stick to buying the best company in any industry.

From the outside at least, Credit Corp is a well-run business with lots of potential in the US after many years of patient investments, and one of the few genuine beneficiaries of a tougher economic environment.

We sold the last of our shares in **South32** on valuation grounds and **Crown Resorts**, as the share price closed in on Blackstone's takeover offer price. The takeover has since received further approvals, while ex **Tyro** CEO Robbie Cook is running from one basket case to another after becoming **Star Entertainment**'s new CEO.

The problems at Star are fixable and Cook knows exactly what's required. There's also plenty of value in the stock. The share price reflects little value for its casino licenses and border openings, the return of international visitors later in the year and the impending completion of the new Brisbane casino bode well for profits and dividends.

We started a small position in **Domino's Pizza** after its share price halved from ludicrous levels. It's one of Australia's genuine global success stories and has the capacity to grow profits and dividends quickly over the next decade.

It's also one of the best managed businesses on the ASX and we look forward to making it a large position as the valuation becomes increasingly attractive.

Our pair of coal stocks, **Whitehaven** and **Newhope**, are minting money at current coal prices. Despite taking some profits to keep risks in check, they still look cheap.

Frontier Digital Ventures released another excellent set of quarterly numbers. Founder and CEO Shaun Di Gregorio is investing heavily in the company's fledgling businesses, as more mature businesses like Zameen start enjoying much higher profits and margins.

In local currency, Zameen's revenue increased 65% over a year earlier while operating profits doubled, lifting the operating profit margin from 10% to 17%. We expect the same trajectory from Frontier's other businesses over the ensuing years now that they're all capable of handling property transactions. They account for more than 50% of Frontier's revenue and it's a much bigger market than property advertising.

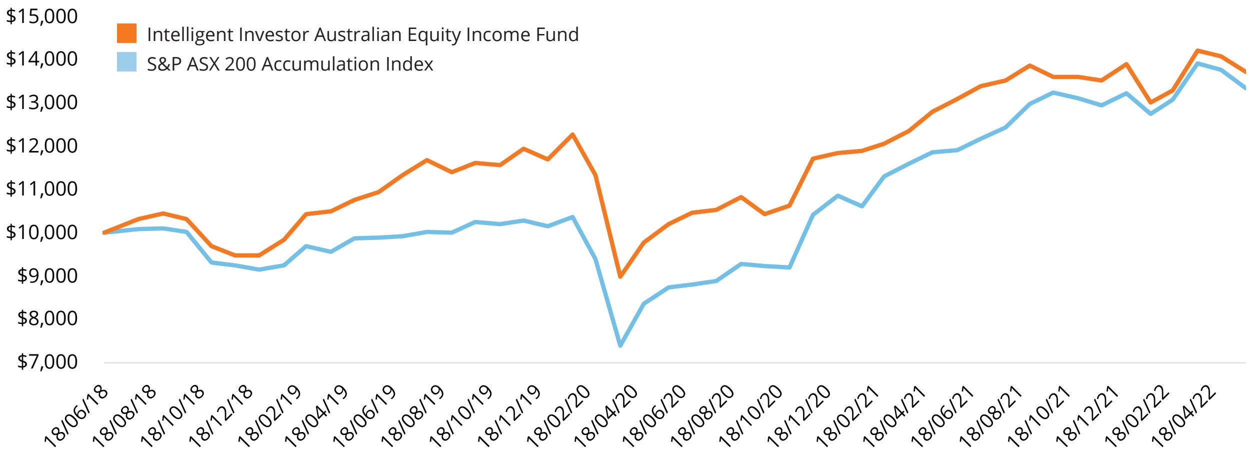
We expect the June quarter to be even better than the March quarter when the results are announced in late July.

LendLease's share price has been weak as the market focuses on the risk of a global recession, but it got a little kick early in the quarter after an activist shareholder's letter to the company justifying a $25 share price was widely reported in the media.

We agree with that potential, as development profits are expected to increase quickly as the world's major cities reopen after COVID lockdowns. But keeping costs down, which is a key plank of new CEO Tony Lombardo's strategy, will be difficult in such a highly inflationary environment.

Please get in touch if you have any questions on **1300 880 160** or at **info@intelligentinvestor.com.au**

Performance since inception



Inception (S.I.): 18 Jun 2018

Asset allocation

Materials	20.1%
Consumer Discretionary	14.9%
Energy	12.1%
Cash	11.1%
Financials	10.3%
Real Estate	9.8%
Information Technology	8.7%
Industrials	5.4%
Health Care	2.8%
Utilities	2.7%
Communication Services	2.1%

Top 5 holdings

BHP Group (BHP)	10.4%
Woodside Petroleum (WPL)	8.8%
RPMGlobal Holdings (RUL)	6.3%
Auckland International Airport (AIA)	5.4%
Star Entertainment Group (SGR)	5.1%

Fund Stats

Income yield	12.99%
Net asset value	$2.62

Important information

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All tables and chart data are correct as at 30 June 2022.