Quarterly Update

30 June 2023

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

Issued by
InvestSMART Funds Management Limited
ACN 067 751 759
AFSL 246441

Managed by
Intelligent Investor Holdings Pty Ltd
ACN 109 360 983
CAR 1255 838

ARSN 620 031 414
ASX Code: INIF

"The desire for more, the fear of missing out, the tendency to compare against others, the influence of the crowd and the dream of the sure thing – these factors are near universal. Thus they have a profound impact on most investors and most markets. The result is mistakes, and those mistakes are frequent, widespread and recurring. Rather than trying to figure out the future, try to figure out where we are in the market cycle, make adjustments if necessary when close to the extremes, and prepare mentally to avoid behavioral mistakes that plague investors throughout. The key is to watch for investor behavior that typically emerges, especially at the extremes of the cycle."

— Howard Marks

The Fund had another good year backing up last year's 10.9% outperformance with a 10.6% return. Though it never feels as good when the market does better. It increased 14.8%.

The changes that we made following our worst period of underperformance in early 2019, such as a cornerstone holding in **BHP** and focusing on companies that can grow their dividends much faster than the market's dividend heavyweights (e.g. the banks, A-REITs and iron ore miners), continues to pay dividends.

Early in the month we swapped **The Lottery Corporation** on valuation grounds for **CSL**, which trades at the most attractive valuation in years due to the share price treading water for nearly the past four.

Performance (after fees)

	3 mth	1 yr	2 yrs p.a	3 yrs p.a	4 yrs p.a	S.I. p.a
II Australian Equity Income Fund	–1.3%	10.6%	7.4%	16.9%	9.1%	7.0%
S&P ASX 200 Accumulation Index	1.0%	14.8%	3.6%	11.1%	6.1%	7.5%
Excess to Benchmark	–2.3%	–4.2%	3.8%	5.8%	3.0%	–0.5%

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

Showing our inability to time markets has never improved, CSL obliged with its first profit downgrade in over a decade. Albeit mainly due to currency movements.

As we show in our annual webinar, CSL has been an incredible growth and income stock over a long time and we're delighted to add it to the fund to complement some of the high yielding but slower growing stocks, such as BHP, **Woodside Petroleum** and **Newhope Coal**.

Portfolio

Newhope paid a final fully franked dividend of 40 cents for an annual fully franked yield of 20%. It followed an excellent quarterly production and financial result, though energy prices have fallen heavily so the large capital gains are likely behind us.

MA Financial's share price has bounced with improving market sentiment and the acquisition of a group of marinas for $225m that will seed a new fund. This is exactly the sort of niche deal we expect from the company but over time the deals will need to get bigger to move the needle on profits.

James Hardie Industries' share price increased after recent results met expectations and signs the drop in US housing starts has bottomed. Not enough new homes are being built in the US so, recession or not, this should fuel the company's profits for decades to come.

Tabcorp's share price also rallied as it remains in the box seat to retain its Victorian wagering license, but it still isn't factoring in favourable tax changes that we expect in the years ahead.

Telstra's share price has reached levels not seen since 2017. It's been a solid performer for the fund but is no longer cheap unless it can sell some assets at higher-than-expected prices. Mobile price hikes and less competitive markets are helping profits, but we look forward to replacing it with a new opportunity.

Sonic Healthcare is increasing its scale in Germany and Switzerland after announcing a couple of tuck-in acquisitions. This is the company's bread and butter, and we expect more as its earnings grow steadily over time.

Star supernova

We reduced our position in **Star Entertainment** after the company announced things are getting even worse. So bad, in fact, that CEO Robbie Cooke announced 500 job cuts and called in the bankers and everyone else with an interest in the company to pull together to save what's left of the Star Sydney casino lest it be sold for its land and building value alone.

Management should've divulged more about Star's rapidly deteriorating operating performance when it recently raised money instead of offering feeble excuses a month later.

It can be a fine line between patiently backing your analysis, and stubbornly hanging on despite a fluid and deteriorating situation. But to borrow a line from Bud Fox in my favourite movie, *Wall Street*, 'the break-up value is higher'.

Though Star isn't at the point of being broken up and sold off in pieces yet, we're managing any ownership bias on our part with a smaller position.

The current situation feels reminiscent of when we upgraded **Aristocrat Leisure** in 2009 at $6.96. I castigated myself for years after it fell below $2 before increasing seven-fold from my initial upgrade and 25 times from the bottom.

It was a similar story for **Fisher and Paykel Healthcare**. Both of which we foolishly sold so early in their recovery that it's comical.

The difference is that Star doesn't have that sort of potential and various government agencies will soon determine Star Sydney's value. Star's destiny isn't entirely in its own hands, which warrants a smaller position.

Pain on the frontier

Like Star Entertainment, **Frontier Digital Ventures**'s (small) capital raising smashed its share price. But a provisional funding deal between Pakistan and the IMF suggests there is still potentially $300m or more of value in Zameen and Pakwheels, twice Frontier Digital's current market value, which obviously isn't factored into its share price given the high risk Pakistan eventually defaults.

Throw in the Latin American (Latam) business that's cashflow positive and could be five times more valuable to Frontier than the Pakistan businesses and you're getting a lot of potential for 40c per share.

The better Latam performs, the less likely there will be another capital raising unless it's for an acquisition. Though it'd be tough to find an acquisition offering better value than Frontier itself at current prices.

The current valuation is particularly pessimistic given its run by a guy who sold his previous business, iProperty, to his former employer, **REA Group**, for over 27x revenue, and has an incredible track record.

In contrast, Frontier currently trades for around three times the revenue of Latam alone, or nearly half what Latam's new management recently struck their company shares at.

Lastly, **Mineral Resources**' share price fell after announcing lower production estimates from its mining services division as contracts expire, and production expansion delays and higher costs at its key Mount Marion lithium project.

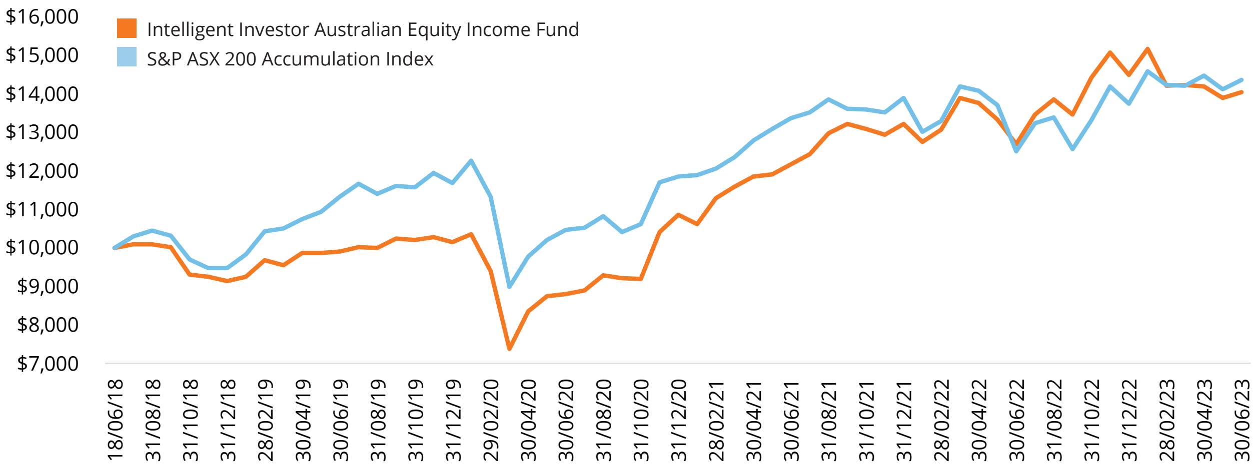
In such a complicated business with numerous divisions, earnings will jump around in the short-term. But, most importantly, we remain comfortable with the company's long-term plans. Hopefully increasing lithium supply will soon give us another buying opportunity.

In addition to the good performance of most of our holdings, there are still several stocks that aren't paying anywhere near the dividends they're capable of due to the lingering effects of Covid and other issues.

As dividends are gradually restored, we expect stocks such as **Auckland Airport**, **Alumina** and Star Entertainment, to provide respectable if not very large capital gains as well.

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	26.6%
Consumer Discretionary	16.6%
Financials	10.2%
Cash	8.4%
Energy	7.8%
Industrials	7.1%
Health Care	6.4%
Information Technology	6.3%
Real Estate	4.3%
Communication Services	3.3%
Utilities	3.1%

Top 5 holdings

BHP Group (BHP)	12.2%
Auckland International Airport (AIA)	7.1%
New Hope Corporation (NHC)	4.8%
Tabcorp Holdings (TAH)	4.7%
RPMGlobal Holdings (RUL)	4.7%

Fund Stats

Distribution yield	8.62%
Net asset value	$2.67

All tables and chart data is correct as at 30 June 2023