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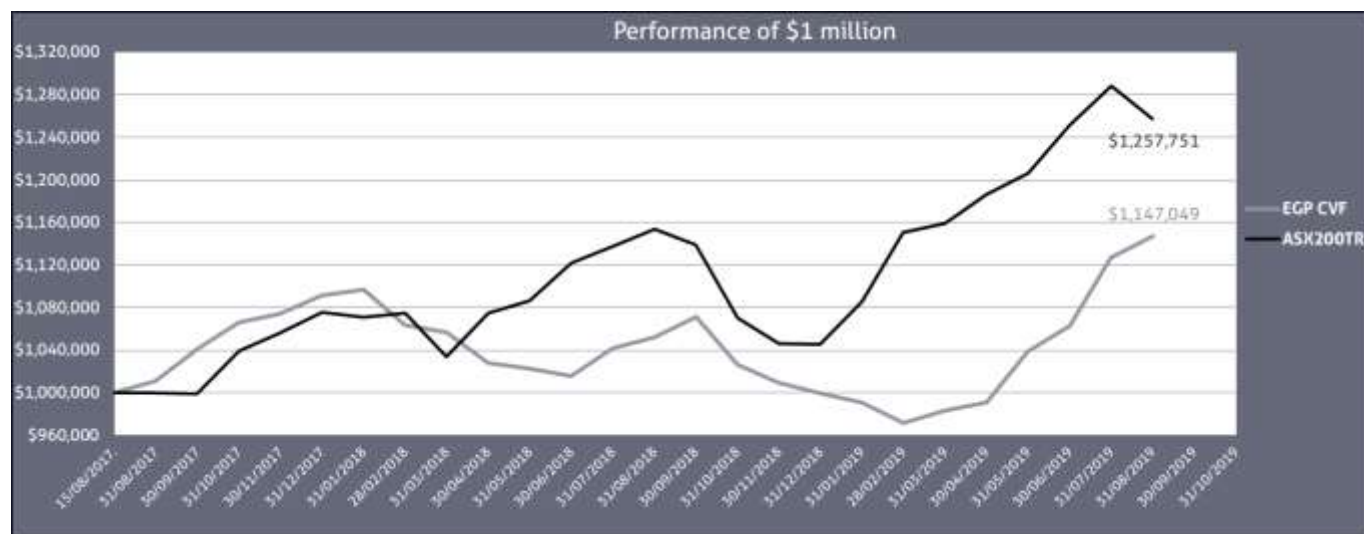
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## EGP Concentrated Value Fund – 31 August 2019

EGP Concentrated Value Fund is a managed investment scheme focused primarily on owning Australian listed businesses. It targets 3 – 5% annual outperformance of Australia’s preeminent ASX200 index over the long term. Managed by a performance oriented co-owner, we run a portfolio that is genuinely different. The sole objective is to deliver the strongest possible risk adjusted returns. The fund manager has their entire investable asset base in the fund, meaning focus on risk is unusually intense.

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	FYTD
EGPCVF FY18	N/A	1.1%*	3.0%	2.4%	0.8%	1.6%	0.5%	(3.0%)	(0.7%)	(2.7%)	(0.6%)	(0.7%)	1.58%
Benchmark FY18	N/A	(0.1%)*	(0.0%)	4.0%	1.6%	1.8%	(0.5%)	0.4%	(3.8%)	3.9%	1.1%	3.3%	12.18%
EGPCVF FY19	2.6%	1.0%	1.8%	(4.2%)	(1.7%)	(1.0%)	(0.9%)	(1.9%)	1.2%	0.9%	4.8%	2.3%	4.63%
Benchmark FY19	1.4%	1.4%	(1.3%)	(6.1%)	(2.2%)	(0.1%)	3.9%	6.0%	0.7%	2.4%	1.7%	3.7%	11.55%
EGPCVF FY20	6.1%	1.8%											7.93%
Benchmark FY20	2.9%	(2.4%)											0.52%

\*August 2017 is the period from August 15<sup>th</sup>-31<sup>st</sup> for both the fund and the benchmark in the above tables.



### The Month That Was:-

The fund rose by 1.8% in August. Our benchmark fell by (2.4%).

The remarkable recent run in our benchmark finally faltered in August. The ASX200TR has now returned “only” 20.34% calendar 2019 to date.

EGPCVF backed up its best month of absolute returns in July 2019 with its best month of relative returns in August 2019 as we bested the benchmark by more than 4%. Reporting season was generally strong for our holdings with most of our reporting companies delivering to or better than our expectations with only a couple of exceptions.

## Results Snapshot:-

Strong results included Shriro Holdings, with the decline in the appliances business now stemmed, the business should pay an 8c fully franked dividend in FY20 and trades on around 8x earnings with a rock-solid net cash balance sheet. United Overseas Australia also produced its customary strong result, producing \$49.1m of NPAT (up 14%) with no revaluation gains and "General and Administrative Expenses" consuming only 75.7% of recurrent (rental, car-parking & hotel etc) earnings, meaning every dollar of (the very substantial) development profits falls straight to the bottom line. UOS trades at about 75c with conservatively stated NTA of \$1.032 per share and just about the most bulletproof balance sheet you're ever likely to see with cash levels above \$400m as a couple of long-lived major developments approach completion and cash starts to gush from the receipt of progress payments.

Weaker than expected from SRG Limited and Consolidated Operations Group are offset by what are likely to be breakout years for both businesses. We feel like both theses are intact.

The results from Lawfinance still look horrendous on a statutory basis (as expected) as the effects of AASB9 continue to defer profitability into future periods. Interestingly, an investor presentation released on September 2<sup>nd</sup> increased the forecast expected collections from the legacy litigation funding portfolio from US\$14m to US\$20m. AU\$9m is a material upgrade in terms of the LAW equity valuation of sub-\$30m. The stock went down on the day of that presentation...

## Welcome to the Boomtown (A Site for Sore Eyes):-

We have at several points intended to write about Site Group Holdings (SIT.ASX), which is now our second largest holding after a spectacular run in August. We were however continually delayed as our understanding of the scale of the opportunity and the chance to put more of our funds to work in what is a truly rare opportunity.

Despite this seemingly being a big reveal of a long "undisclosed" top 10 holding, we actually described the early iteration of our thoughts on the SIT opportunity in the FY2018 annual letter, we wrote:

*One other interesting business I thought I would touch on in this year's report is Site Group International (SIT.ASX). SIT sits just outside of our top 20 holdings and is sized that way because there are much bigger risks than our largest investments. With that said, the upside is also significantly bigger than most of our larger holdings.*

*SIT is an education provider; it presently has a market capitalisation of around \$17m. They had a VET Fee HELP business that was severely impacted by the industry-wide debacle that industry suffered as the poorly constructed scheme imploded due to widespread exploitation by unscrupulous operators. In our view, SIT provided quality programs that met the intended function of the scheme, but their business was destroyed anyway when the scheme was shuttered. As a consequence of this, the company had recorded in its FY17 accounts a payable due from the Department of Education and Training (DET) of almost \$34m. An initial disbursement against that debt of \$4.9m was approved in December 2017. This leaves an outstanding debt due from DET of about \$29m, which we view as highly likely to be paid in the fullness of time.*

*The Australian Skills Quality Authority (ASQA) recently cancelled SIT's licence to operate in Australia. This looks (to an industry outsider) a leverage gambit to try to settle the claim with DET. There is no indication SIT have ever failed to deliver on their promises in respect of their licence. SIT have obtained a legal stay of the cancellation which allows them to continue operating until a hearing/mediation can be held. Their Australian business in the meantime is suffering as many major employers are reluctant to use a provider with such an issue over their licence.*

*SIT also has a substantial and growing international business, which is, in my view, where the future for the business lies. The international business is generating less than \$20m per annum in revenues at present, but is fast growing and has good margins.*

*As part of their international strategy, SIT controls a 30 hectare piece of land in the Clark-Freeport area of the Philippines, near Clark International Airport. The training facility in Clark only utilises about half of the land footprint and in light of the difficulties the DET & ASQA have caused the Australian business, SIT have begun investigating ways to monetise the 15 hectares in excess of their needs.*

*Vacant land in nearby areas has recently been fetching between US\$2m-5m per hectare depending on location. Interests associated with their Philippine based director Nic Alcantara have loaned SIT US\$4m which can either be repaid or taken in equity at 4cps (60% above the 30 June 2018 closing price of 2.5cps). Mr Alcantara has been tasked with monetising the asset. He will receive 5% of the project value with an additional 5% if a valuation in excess of US\$30m is obtained.*

*I have no particular expertise in Philippines industrial property, but I'd hazard Mr Alcantara would have agreed the incentive point of US\$30m because he believes it is achievable.*

*In any case, if SIT can realise the majority of the \$29m the DET owe them, and US\$27m (US\$30m less the 10% incentive payment) for the excess land in the Philippines, then potential cash payments of AU\$65m could be due to SIT. This amount roughly quadruples the current market capitalisation of the business, or about 10cps of cash. Shareholders would also still own the Australian and International education businesses, which would be well placed to succeed if the business had that kind of cash firepower to realise their ambitions.*

Our holding in SIT was just outside our top 20 at the time I wrote that, it is now our 2<sup>nd</sup> largest holding, partially through an increase in valuation, but mostly through our adding to the position as we became more certain of the likelihood of realising a valuation meaningfully above our initial expectations (which were fairly high).

I visited Clark in March this year, which was enormously helpful in better understanding the way the piece of land is presently used by SIT. I wrote in the piece quoted above that SIT use about half of the 30 hectare site, which is true, but only because the sprawling site (it was the part of the site for [Expo Pilipino](#)), the same delivery of services could probably be delivered on perhaps 3 hectares of land if it were more judiciously used, they use half the site, but only because they can, not because they need to.

I also met with a number of different people and organisations as I sought to better understand the likelihood of a really significant outcome from the land asset. I have met or communicated with developers, real estate agents, land owners, representatives of commercial real estate services businesses, town planners and others to understand as best I can the likelihood of a positive outcome in respect of the transaction SIT is seeking.

The exact nature of the transaction the company will do has not been disclosed. My impression is that a full range of options are being assessed, with everything from a full sale of the land-holding to a partial sale of some of the site, to partnering with a developer, with them perhaps taking a majority interest in the land and SIT retaining some type of upside exposure to the development profits achieved over time. As long as they maximise the shareholder value, an incredible opportunity exists.

The key reason the holding has become such an important one for the fund is that I am now quite certain that the land is an enormously valuable asset and a significant realisation of some or all of that value is quite imminent. My current expectation is that there will be a transaction in FY20 for the land. My previous "base-case" valuation for the likely value received for the asset, which was US\$30m

(based on the [agreement signed](#) with Philippines based director Nic Alcantra). I am now of the opinion that a valuation of at least US\$90m is likely, based on recent nearby transactions and discussions with parties aware of where the market stands in the area.

The current market capitalisation of SIT is \$45m. At current exchange rates, if 100% of the land and the US\$90m price I now think is a floor valuation were achieved, more than AU\$130m would be received by the company (before transaction costs). Assume even (a very high estimate) \$20m leaked via costs, the remaining \$110m amounts to a potential cash hoard of 14 cents per share, given the current shares on issue. Our sincere hope as a meaningful equity holder in SIT is that a bidding war breaks out. There is a limited land footprint inside the Clark-Freeport special economic zone and this appears to be the last large parcel of land that is available for private acquisition. This area is a genuine boomtown and the scale of development needs to be seen to be believed.

Given CEO Vern Wills owns a significant portion of the business and has contributed an enormous amount of his own cash to the business over the years, I am certain he is keen to do a deal that will maximise the long term value SIT shareholders will receive, rather than just cash in the asset to the highest bidder. This will quite possibly involve retaining some exposure to the Clark asset. I have no specific knowledge of the negotiations taking place, but my expectation is that any developer would likely want to put their foot on a majority interest in the Clark land. I would expect they would want to own at least 60%, possibly as much as 80% of the land if they were to retain SIT as a joint venture partner. They would likely still need to make a significant cash payment to SIT in order to take this stake. Assume they wished to acquire a 2/3<sup>rd</sup> interest in the land, this would require a payment of something exceeding US\$60m, or 9-10cps of cash. I have asked the CEO what his intentions would be in the event that a significant value was realised for all or part of the Clark asset. He indicated given what a tough experience shareholders have had over the past 3 or 4 years, that the equitable thing to do would be to return a significant portion of any funds received to shareholders in some form of capital return or dividend. In the 9-10c cash realisation scenario described previously, I would hope to see at least 4 or 5 cents per share of cash returned to shareholders.

Such a decision would also leave 4 or 5 cents per share for the business to execute on the three key value creation opportunities they would have ahead of them at that point. The first opportunity, which would require the least time and funding, would be the pursuit of a litigation outcome in the case against DET. Most of the delays in finalising the matter have been legal, but I would hazard that a significant bank balance would see the timeline of the case accelerated and the likelihood of a successful outcome to SIT meaningfully improved. It would be nice if they were able to get most or all of the >\$20m the company is owed, but any reasonable financial outcome realised from the process would be a good result for shareholders.

The second is the incredible opportunity in the international education business. The company now has three "safe live process plants", one each in Myanmar, Papua New Guinea and Philippines (this short [YouTube video](#) shows what a SLPP is). These SLPP's are providing incredible educational outcomes and there is enormous demand for these wonderful teaching tools in new locations. Capital availability has been the key constraint for SIT thus far. With some cash freed up by monetising the Clark land asset, more SLPP's can be built and they have outstanding financial characteristics, with an expected payback period of less than 2 years. The SLPP's are just one part of the SIT international business, with the right funding available, I would expect the international education business could do \$50-70m of revenue within a few years at EBITDA margins that should exceed 20% and may be as high as 30% depending on the mix of revenues.

The third opportunity is the remaining interest in the development of the Clark asset. It is very hard to speculate on the type of value that could be created from the asset, and the level of capital that might be required from SIT to fund their share of such an opportunity until we better understand any deal that is done. It remains possible that a blockbuster offer for the entire landholding is made and this becomes a moot point, but retaining an interest with the right partner could see an opportunity for significant long-term gains. Given the significant shareholding CEO Vern Wills holds, we are sure he will think strategically about the best way to realise the greatest value.

The key problem for SIT is the Australian operations, which are losing money and appear to be unlikely to be able to be remedied, certainly not before a legal resolution is reached in the matter with DET. Given the much better opportunity for the international business, we are hopeful that the Australian business can be sold at some point to remove the distraction and enable the business to focus on its best opportunities. Unfortunately, this is probably sometime away.

For now, SIT has recently raised sufficient cash to ensure it is able to execute on the land transaction. The resolution of that will in turn inform the scale of the opportunities the remaining business can deliver.

### **Key Portfolio Information:-**

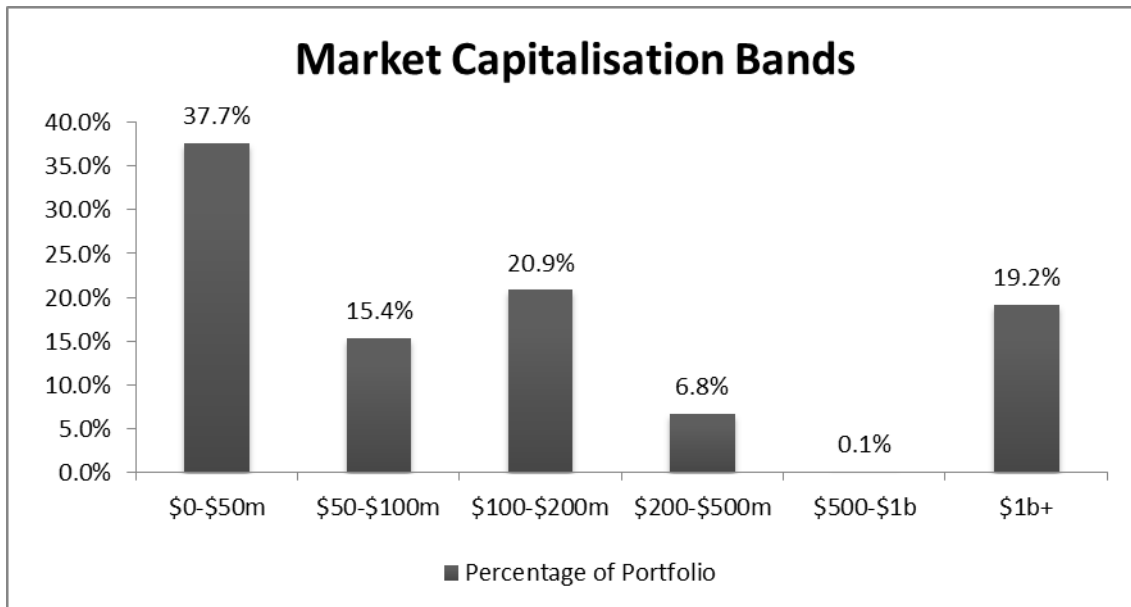
Our top 10 holdings at 31 August 2019 were:

Rank	Holding	Percentage Equity Weighting	Percentage Portfolio Weighting
1	United Overseas Australia (UOS.ASX)	13.9%	11.4%
2	Site Group International (SIT.ASX)	11.8%	9.8%
3	Kangaroo Plantation (KPT.ASX)	8.1%	6.7%
4	Dicker Data (DDR.ASX)	5.3%	4.4%
5	LawFinance (LAW.ASX)	4.7%	3.8%
6	Blackwall Limited (BWF.ASX)	4.1%	3.4%
7	SRG Global (SRG.ASX)	3.8%	3.2%
8	Locality Planning (LPE.ASX)	3.6%	3.0%
9	Konekt (KKT.ASX)	3.0%	2.4%
10	Undisclosed	2.8%	2.4%

Our largest 5 holdings now comprise 43.8% of our invested capital, our top 10 holdings are 61.1% and our top 15 represent 73.4%. Cash and cash equivalents are 17.5% of the portfolio.

The market capitalisation graph is set out overleaf. This month, the median market capitalisation is \$92.2m.

## Market Capitalisation Bands



As always, investors with any questions, suggestions, comments or investment ideas should feel free to drop me a line – [Tony@egpcapital.com.au](mailto:Tony@egpcapital.com.au)



Fund Features		Portfolio Analytics	
Min. Initial investment	\$50,000	Sharpe Ratio <sup>1</sup>	0.64
Max. Initial investment	\$2,000,000		
Additional investments	\$5,000 (Minimum) \$200,000 (Maximum)	Sortino Ratio <sup>1</sup>	0.43
Applications/redemptions	Monthly	Annualised Standard Dev. – EGP	8.25%
		Annualised S/D - Benchmark	9.37%
Distribution	Annual 30 <sup>th</sup> June	Largest Monthly Loss – EGP	-4.2%
		Largest Monthly Loss - Benchmark	-6.1%
Management fee	0%	Largest Drawdown – EGP	-9.4%
		Largest Drawdown - Benchmark	-9.4%
Performance fee (<\$50m)	20.5% (inc GST)	% Of Positive Months – EGP	60.0%
Performance fee (>\$50m)	15.375% (inc GST)	% Of Positive Months - Benchmark	64.0%
Auditor	Ernst & Young	Cumulative return <sup>2</sup> – EGP	14.7%
		Cumulative return <sup>2</sup> – Benchmark	25.8%
Custodian/PB	NAB Asset Services	1 year return <sup>2</sup> – EGP	9.0%
		1 year return – Benchmark	9.0%
Responsible Entity	Fundhost Limited	3 year annualised return <sup>2</sup> – EGP	N/A
		3 year annualised – Benchmark	N/A
Fund Size	\$63.1m	5 year annualised return <sup>2</sup> – EGP	N/A
		5 year annualised – Benchmark	N/A
Mid-Price for EGPCVF Units	\$1.0428	Buy Price for EGPCVF Units	\$1.0444
Accumulated Franking per Unit	\$0.0079	Sell Price for EGPCVF Units	\$1.0412

<sup>1</sup> Sharpe and Sortino Ratios calculated using the Monthly Benchmark ASX200 Total Return Index

<sup>2</sup> Return is net of all fees and costs and assumes reinvestment of dividends. 1, 3 and 5 year figures are rolling annualised figures.

Past performance is not an indicator of future performance.

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