

## Strategy Notes January 2017– A Fishy Business

One of the real pleasures of investing within the emerging companies space is the ever-evolving variety of businesses and industries we come across in our constant search for new ideas to allocate our investor capital. Where businesses inside the Top 50 are generally well established in industries that are well known and understood by fund managers and broker analysts alike, the small cap space requires us to get out and understand new industry sectors constantly as new opportunities arise.

15 years ago (pre-CSL), not a great deal was probably understood by local investors about the global blood plasma industry, whereas now any local healthcare analyst will have a complete understanding of plasma pricing and the broader immuno-oncology space. For the small cap investors, many would not have fashioned a complete understanding of the behavioural shopping habits of the Chinese consumer pre-2013, however after the success of Bellamys (initially), A2 Milk and Blackmores the majority of the industry can now wax lyrical about the importance of the *daigou* and the brand preferences of Chinese mothers for the nutrition of their children.

Larger businesses as they grow typically take on more conglomerate-type structures, where different units of the business are exposed to various thematic through the economic cycle – this smooths out their returns, but also dilutes the exposure to any one underlying theme. Small cap managers would have undoubtedly licked their lips at the prospect of owning single exposure companies like Domain Real Estate (inside Fairfax), Bunnings (inside Wesfarmers) or Dan Murphys (inside Woolworths) as excellent leveraged plays on structurally growing industries. Unfortunately, while the growth of those businesses has been incredible in the past 5 years, the market caps of the conglomerates they sit inside haven't produced similar returns due to other underperforming business units.

While the ability to invest in emerging companies with singular exposures allows us the opportunity to generate great returns, the leverage of earnings to one sector...

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