

## Strategy Notes November 2017– A Q&A with Senior Portfolio Manager Steven Ng

It was a pleasure this month for Steven Ng to sit down with James Marlay from **Livewire Markets** for a fairly broad-ranging interview to cover off on the five-year anniversary of the Ophir Asset Management business and thoughts on the business and current investing climate. The interview is ~25min in length and covers a variety of topics and companies, including Stevens early investment background, some specific sector and company commentary and broader views on the outlook.

For the interest of readers of our Letters, we have included some edited comments to a number of questions below, however the full video interview can be accessed via the link below. We hope you enjoy.

<https://www.livewiremarkets.com/wires/ophir-growth-hides-all-sins>

**James Marlay, Livewire Markets:** *Steven, can you give us a quick background on how you got started in investing and what your introduction to the skillset was?*

**Steven Ng, Senior Portfolio Manager:** I was quite a late bloomer coming into this industry – my background was initially in accounting and then I moved into management consulting with Bain International where I did secondment work at Diageo. Really at that point in time I was able to see the full spectrum of what was available in terms of corporate work – on the one hand there was fantastic opportunities dealing with CEO's at a strategy level and then at the same time there was also the real minutia of detail that you could get into working within a corporate.

Really what I wanted to do was try and find something where I could blend the two and pick the relevant skill sets out of that. So when I scanned the landscape and had that 'epiphany' moment of what next for my career, investing was one of them. And through some hard work, a bit of determination and a bit of luck I managed to break into the industry and join the Macquarie small cap team back in 2001.

**James Marlay:** *You've worked at Macquarie and also at the well-regarded Paradise Investment Management. What have been some of the lessons picked up through your experience at those groups?*

**Steven Ng:** The key learning I've had from my time there is that the number one criteria in investing is always passion. You don't have to be the smartest, you don't have to be the hardest working – you just have to be the most passionate person that is always going to go over and above in terms of trying to get that next big idea or get that edge on that stock and really following through. So if there's one thing it's passion.

The second thing I learnt from working at both those shops is backing your conviction in the calls. There's going to be times when the market is right and there's also going to be times when you're right. And that's when you really separate the men from the boys. Standing up against the market and proving that your analysis is correct and really following through – that's when you make the best investments of all.

**James Marlay:** *High conviction is a stamp of your investing style. Can you go into some more detail around how you think about 'high conviction', concentration and the overall philosophy of how you approach the market?*

**Steven Ng:** Look, you can have your traditional small cap portfolio and that's generally been a portfolio consisting of 40 or 50 stocks that sit within it. But it's probably fair to say it's been proven many times that a portfolio of 15 to 20 stocks provides enough diversification for you in any portfolio that you have. So I'd always challenge any manager and ask 'do you really have that much

conviction in your 50<sup>th</sup> or 60<sup>th</sup> stock? Is it really going to add that much incremental contribution to your portfolio?' I'd say it's probably unlikely. If anything, it just adds extra noise to the process.

What we really like doing is backing ourselves, backing our analysis, doing that extra bit of homework that no one else has done and really knowing the companies better than anyone else. What we like about our High Conviction Fund is that every stock counts. We've got high conviction in the stocks, we've got high conviction in what they can grow into and how big they can be. It's really backing those people and backing those management teams as part of that journey.

**James Marlay:** *Commentary in major newspapers around the economy are currently more focused on the negatives. From your interactions with management, do you think that's overcooked? Or are things bubbling on OK?*

**Steven Ng:** We're always going to have a positive bias because we're always talking to companies that are either growing or that we think are going to do well, so we are mindful that we have a more selective subset. We've spoken previously about areas that are broadly doing well – IT, companies exposed to mining services, those exposed to any infrastructure spend, travel businesses etc. On the other side, sectors like retail continues to be tough – we saw recently Speciality Fashion closing 300 stores out of a store footprint of 1000. That's sending a very big signal to mall owners in Australia.

I think conditions broadly remain difficult at the moment, however we remain very optimistic about the companies we own. We only have to look at our portfolio at the moment where we have north of 50% of the earnings of the portfolio generated overseas now. When I started in the industry in 2001, having overseas exposure was generally seen as a negative. People used to put those companies on a discount because of what could happen – generally something always went wrong, it was too far away from Australia and we didn't generally travel overseas. It was never really considered a growth option or deserving of a premium.

Roll forward to now in late 2017 and you have all these fantastic businesses with overseas growth options, the markets are infinitely bigger than Australia's population of 20 million – it just becomes exciting. You only need to capture one or two per cent of a very big market as opposed to twenty per cent of a tiny market and you can have a fantastic outcome for the business and its growth profile.

**James Marlay:** *Are companies able to grow domestically?*

**Steven Ng:** Sure, there's companies currently experiencing a rapid rate of growth that we historically have never seen in Australia due to the advent of technology. Think about a company like AfterPay that only started a couple of years ago and has gone from miniscule sales of a couple of million dollars to now processing on an annualised basis north of \$2bn of retail sales, all predominantly online. That is a phenomenal effort and they've executed flawlessly. They're now processing north of 25% of all online sales at the moment and maybe 5% of total retail sales – that's a truly phenomenal outcome for any management team to have executed on.

They're essentially helping retailers take on Amazon – the average basket size is higher, the conversion size is higher, you're driving traffic to the retailer's website. It's incredible stuff for a business that didn't even exist four or five years ago.

**James Marlay:** *High growth, high PE's and high expectations can be a recipe for a bumpy ride. Is it part and parcel of what you're doing?*

**Steven Ng:** Ultimately we take a balanced approach to our portfolio and while we do have some higher growth names in there we ultimately always look at valuation. The key criteria for our investments methodology are: 'is the company a good company and can it grow into a big market?'; 'does it earn a good return on capital in terms of how much we give to it?', and, most importantly, 'does it have a good balance sheet?' We immediately screen out a lot of companies that we believe

are too conceptual in nature or are in something that we'll never be able to understand meaningfully or be able to gain an edge on.

**James Marlay:** *Limiting capacity is often cited as an important part of the investment structure at Ophir. Can you talk a little more about the structure and why the Funds are eventually closed to investors?*

It's a fair question to ask why do we close the Funds. One of the key elements that we always like to leave behind with our investors is that alignment and passion are the two characteristics of what you'll see in anybody that works at Ophir. Andrew and I have the majority, if not all, of our personal wealth invested within our Funds so we're very aligned with our unitholders. What we're motivated by, and what we're passionate about, is delivering performance – not only for our unitholders but also ultimately for ourselves.

We see our investment in the Funds as a long-term compounding vehicle for us to create wealth and so limiting the capacity, or size, of the Funds will better provide that ability to do that. We've seen other examples where managers effectively become asset collectors in the space and over time that makes outperformance difficult. So we're very disciplined in terms of managing the capacity, and ensuring that the capacity remains the asset of our clients. We feel if we maintain the capacity and are strict in terms of the capital we take in, then we're always going to give ourselves a fighting chance to outperform.

**As always, thank you for entrusting your capital with us.**

Kindest regards,

Andrew Mitchell & Steven Ng

Co-Founders & Portfolio Managers

Ophir Asset Management

*This document is issued by Ophir Asset Management (AFSL 420 082) in relation to the Ophir Opportunities Fund & the Ophir High Conviction Fund (the Funds) and is intended for wholesale investors only. The information provided in this document is general information only and does not constitute investment or other advice. The content of this document does not constitute an offer or solicitation to subscribe for units in the Funds. Ophir Asset Management accepts no liability for any inaccurate, incomplete or omitted information of any kind or any losses caused by using this information. Any investment decision in connection with the Funds should only be made based on the information contained in the Information Memorandum and/or Product Disclosure Statements.*