4.8%

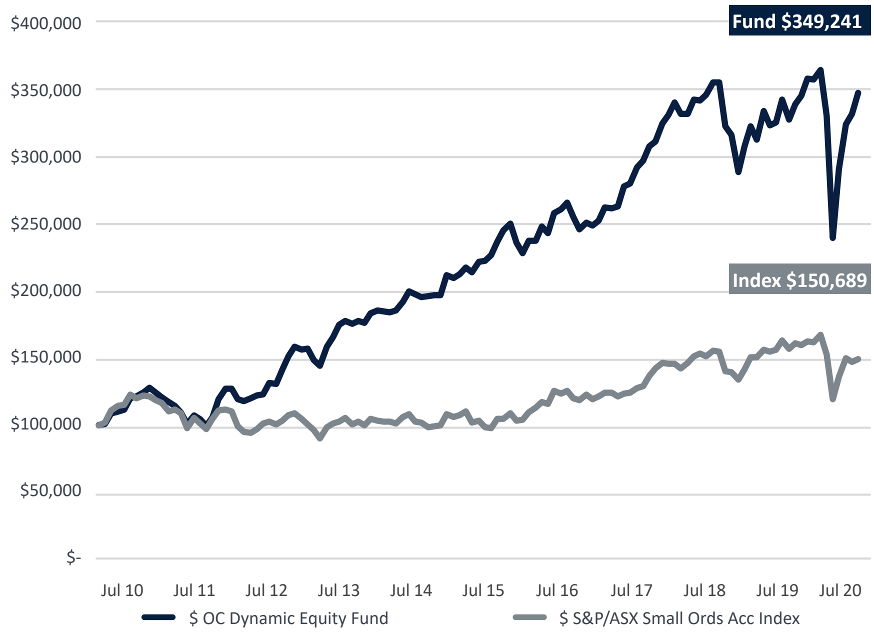
Fund up 4.8% for the month

13.4%

Returned 13.4% p.a. for the past 10 years

We remain confident the Fund will continue to deliver attractive long-term returns

Performance comparison of $100,000 over 10 years[*]



Total returns

At 31 July 2020[†]	1 mth %	3 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	7 yrs % p.a.	10 yrs % p.a.	Incep. % p.a. (Dec 2000)
OC Dynamic	4.8	19.6	1.4	7.5	9.5	12.0	13.4	12.0
S&P/ASX Small Ords Accum	1.4	9.9	-8.5	6.5	7.9	6.3	4.2	5.7
Outperformance	**3.4**	**9.7**	**9.9**	**1.0**	**1.6**	**5.6**	**9.2**	**6.3**
S&P/ASX Small Ind Accum	-0.1	7.0	-10.9	5.3	6.4	7.1	7.9	6.0
Outperformance	**4.9**	**12.7**	**12.3**	**2.2**	**3.1**	**4.9**	**5.4**	**6.0**

The total return performance figures quoted are historical, calculated using end-of-month hard-close mid-prices and do not allow for the effects of income tax or inflation.

Performance review

The S&P/ASX Small Ordinaries Accumulation Index finished the month up +1.4%, which was well ahead of the S&P/ASX Small Industrials Accumulation Index which recorded a small fall of -0.1%. The OC Dynamic Equity Fund finished the month well ahead of both indices, returning +4.8% for the month. This was a strong result given that the Fund does not invest in single commodity, single resource stocks in its core portfolio due to their elevated risk profiles which means that the Fund largely missed the rally in gold stocks during the month. The technology sector was again a strong performer during the month and some of the Fund's smaller positions, several of which are relatively new to the portfolio, did much of the heavy lifting in August.

Life360, Inc. (360, +65.2%) rallied off its lows as the market applauded its quarterly update and a new pool of investors began to analyse this under-appreciated tech stock. OC has been invested in 360 since its ASX listing just over 12 months ago and our experience to date has been disappointing with the stock still languishing below its IPO issue price. San Francisco based, Life360 operates a smart phone accessible platform which aims to bring families together by offering features such as driver safety and group member tracking and has almost 30 million monthly active users. The highlight of the June quarter was the maiden reporting of positive cashflow for the business which was driven by tight cost control and relatively resilient subscription levels demonstrated through the recent period of COVID-19 lockdowns.

The stock performance was helped along by major holder, and oft touted seller of its 360 shareholding, ADT Security Corporation, exiting its 10% stake in the company to new and existing institutional investors later in July. When the market is aware of a large stake being offered for sale, new investors will often wait for the line of stock to 'clear' before buying any stock in the market. This indeed happened with the ADT stake as the stock closed the month almost 10% above the clearing price. We believe 360 is well positioned to capitalise on its market leadership position in North America, and with an expanded product offering and new geographies to move into, we see excellent growth and cash flow generation for 360 moving forward.

Redbubble Limited (RBL, +27.2%) has been a strong performer for the Fund after being added to the portfolio recently with the business a structural beneficiary of the COVID-19 environment. RBL is a leading global online marketplace that enables independent artists to sell their designs on products that are manufactured and delivered via third party fulfillers. It offers its services through both Redbubble.com and Teepublic.com and its geographic markets are predominately North America 62%, Europe 18%, United Kingdom 13% and Aust/NZ 7%. Prior to our investment, the company had been through a series of management changes that had resulted in successive profit downgrades, although the underlying business has continued to grow revenue at +20%.

Founder and major shareholder Martin Hoskin recently returned to the company as interim CEO and business growth has accelerated materially with the recent quarter to date update showing an escalation in both revenue and EBITDA across both its key marketplaces. No doubt the company is a beneficiary of the social-distancing and lock-down restrictions which have driven an acceleration in leading online e-commerce platforms. RBL is also a beneficiary of the work from home dynamic across product categories such as home décor and wall art. The new management team is committed to driving a reduction in the cost of doing business ratio, including headcount and other operating costs, which is currently significantly above other online marketplace peers and should be 'low hanging fruit' and drive better operating leverage across the group. RBL has announced several new product launches of late including facemasks which were launched in late April and have experienced high levels of demand. The company has strong structural tailwinds which, combined with a more concerted focus on operating costs, should see both top and bottom line growth accelerate further in the coming months.

US based "buy now, pay later" (BNPL) **company Sezzle Inc. (SZL, +81.4%)** was again a stand-out with an array of positive news flow, a successful capital raising and broader awareness of the company amongst the investment community all shining a positive light on the company. As mentioned in the OC Funds June Quarterly review, the market has gained an appreciation that the pandemic would help to drive adoption of SZL's offering as online shopping surged in popularity due to social distancing restrictions and consumer fears around shopping in-store. The BNPL segment has two key tailwinds, namely millennial's aversion to credit cards and the growth in the ecommerce channel. SZL's growth was highlighted by record Underlying Merchant Sales in the June quarter of US$188m (+57% quarter-on-quarter and +349% year-on-year). Active customers rose 28% quarter-on-quarter to ~1.48m, active merchants jumped 28% quarter on quarter and leading loss indicators continued to show improvement. The company's customer frequency data (by cohort) demonstrates a similar pattern to larger listed peer Afterpay: SZL's 2018 cohort now transacts 15x p.a., its 2019 cohort transacts ~9x p.a. and its 2020 cohort ~5x p.a. which demonstrates both the growth embedded in the existing customer base and the power of its network effect. SZL undertook a $79.1m institutional capital raising during the month which was heavily oversubscribed. The additional capital gives SZL a long runway to expand its reach in the North American market and we expect to see growth continue to accelerate in the coming months.

Not all companies have been negatively impacted by the COVID-19 induced conditions, with a handful of businesses being thrust into the spotlight as their products gain broader adoption, particularly because of the stringent social distancing regulations now in place. One such company is **Whispir Limited (WSP, +116.7%)** (a pre-IPO holding for the Fund) which listed in June 2019. WSP provides communications systems and workflows primarily centred on mobile messaging. Following a stellar June quarter, WSP again re-rated significantly in July as the market grew a broader appreciation of its business model. The company reported a bumper June quarter as a record number of companies signed onto WSP services to communicate with staff and customers, and government agencies used the service to message persons subject to quarantine conditions. The relatively unknown messaging service is well suited for use in business contingency plans and widespread communications scenarios and has been growing strongly in Australia and abroad. The company remains on track to deliver all its key FY20 Prospectus forecast metrics; notwithstanding, the Fund has reduced its holding into the recent share price strength.

Viva Leisure Ltd (VVA, -14.1%) was a rare underperformer for the Fund over the month of July as further lockdowns in Melbourne affected a small part of the VVA portfolio of gyms (metro Melbourne accounts for just 4% of the total membership portfolio). Perhaps weighing more heavily on the share price is the risk of further lockdowns in NSW and potentially the ACT which could eventuate should the COVID-19 infection rates in those areas continue to spike.

On a more positive note, VVA announced the A$20m acquisition of the master franchisor of the Plus Fitness franchise network in July which has 197 locations across Australia, New Zealand and India. Plus Fitness is predominantly a network of low cost, 24/7 express gyms in Australia, with a geographical weighting towards NSW. VVA management believe there is scope to double the size of the Plus Fitness network, using either franchisee or VVA capital. Whilst the valuation multiple of 8x normalised EBITDA is higher than historic VVA acquisitions, this acquisition provides a captive pipeline of future acquisitions given that VVA has right of first refusal on any acquisitions of franchisees operations which is likely to occur at multiples closer to 3x EBITDA and therefore be extremely earnings accretive. VVA management expect to acquire up to 50 franchisee gyms from the existing network inside the next two years. There are also likely to be material synergies for VVA to extract from these acquisitions given the combined scale of the enlarged network.

Helloworld (HLO, -29.7%) was the key disappointment during the month and suffered as the second wave of COVID-19 infections cast a further shadow over the outlook for the travel industry. HLO is our only remaining travel exposure and has been reduced in the portfolio to a small weighting in recent months. The company raised additional capital late in July in a $50m underwritten institutional share placement and rights issue to which the Fund subscribed. Despite the opaque outlook for the travel industry, HLO has very low operating costs with its franchised model meaning that bricks and mortar operating costs are largely the responsibility of franchisees. The company continues to generate modest revenue of ~$2m per month (much of it from its government contracts) and incurs relatively low operating costs (~$4m average cash costs) so the capital raising will give the company a long run-way of liquidity even in the event of protracted further lockdowns. We believe that the company can operate profitably once the current domestic border restrictions are removed and now has adequate liquidity to operate even if international travel does not return until CY22. Travel stocks are once again in the doldrums as the second wave of COVID-19 pushes out the likelihood of domestic and international travel. But having some small exposure to a travel company that has a long liquidity run-way provides some portfolio insurance in the event that a COVID-19 vaccine is approved ahead of market expectations.

Outlook

Global equity markets continue to trend upward which to many may seem counter intuitive given the mounting social and economic cost of the COVID-19 pandemic. This has been the case for some time now but can be attributed to both the huge central bank and government stimulus programs globally which are cushioning the economic impact of the pandemic and providing an unprecedented liquidity buffer for markets. Given the forward-looking nature of markets, investors still seem prepared to look through the short-term economic damage toward an eventual recovery.

For several months we have flagged a secondary surge in Coronavirus infections as the key risks to the nascent economic recovery that was showing promise in both Australia and several other key markets such as China and the US. The second wave of infections that has recently flared-up domestically, in several US states and in parts of Europe and Asia is of real concern for the long-term global economic outlook. A COVID-19 vaccine is a cause for genuine optimism with several credible candidates demonstrating a promising immune response in small scale, early trials. The results of the much larger Stage 3 double blind studies are due in the fourth quarter of CY20 for several of the leading vaccine candidates. But at this stage they remain mere hope on the horizon with the ultimate outcome of the trials, and the likelihood of regulatory approvals, still largely an unknown.

There is no easy pathway through the pandemic, as policy makers in the West continue to balance competing priorities, being an appropriate health policy approach, against the reality of a market-based economy. US Federal Reserve Chairman (‘the Fed’) Jerome Powell stood by his ‘whatever it takes’ rhetoric during the month by making it clear the Fed’s plan to keep rates at rock-bottom for the foreseeable future: “We’re not thinking about raising rates, we’re not even thinking about thinking about raising rates,” he said. Indeed, the Fed has some heavy lifting to do: the US recession is deep with Q2 GDP plunging 32.9% on an annualised basis after the prior period’s 5% slide, and initial jobless claims are increasing in recent weeks for the first time since March amid accelerating COVID-19 infections in some states. Our own Central Bank, the Reserve Bank of Australia (RBA), continues its proactive response to the pandemic and recently declared it will start buying government bonds to keep the cost of borrowing at record lows.

Victoria has now entered Stage 4 restrictions and there has been an acceleration of COVID-19 cases in both NSW and Queensland. In just six weeks, Victoria has gone from ‘flattening the curve’ to a state of crisis, with state borders closed for the first time in a century and Melbourne, a city of more than five million people, under strict curfew for six weeks. Victoria accounts for about 25 per cent of Australia’s economy and 26 per cent of the population and activity levels are set to plunge. Victoria is home to the nation’s biggest port and key manufacturers and is critical to the supply chain of many businesses and retailers across Australia. Aside from the steep economic toll, the human cost is mounting, both in terms of the sick and deceased but also the huge toll from mental health issues and domestic violence cases.

A key positive during the month was the $20bn extension to the government’s JobKeeper/JobSeeker program, which goes a meaningful way toward reducing the looming fiscal cliff. The ongoing support of the jobs market by the Federal government amid the COVID-19 pandemic helped the small-cap market finish the month higher despite the re-introduction of mobility restrictions in Victoria and further border closures between NSW/Vic and Qld/NSW.

Unfortunately, the JobKeeper/JobSeeker program is insufficient to prevent a large escalation in the unemployment rate, with the second wave in Victoria likely to leave around 400,000 more Australians unemployed and cost the economy up to $12 billion. Eighty per cent of the impact is likely to be felt in Victoria, with the lockdown measures expected to reduce the size of the real economy in the September quarter by between $7 and $9 billion. The RBA now expects that the unemployment rate will hit 10% later in the year and the expected rebound in economic growth will now be much more subdued because of Victoria's second virus outbreak.

The other noteworthy economic headline during the month was domestic inflation print. The consumer price index dropped an unprecedented 1.9% over the three months to the end of June, leaving the annual rate of inflation at negative 0.3%. This is the biggest bout of consumer price deflation in 72 years and only the third time since 1949 that the annual inflation rate has been negative. Childcare, petrol, rents and health insurance premium deferrals, and travel bans, will all contribute to a steep fall in prices in the June quarter. Inflation is a polarising subject at the moment with many, including the gold bugs, adamant that inflation will escalate rapidly in the future as central governments are forced to monetise their debt amid rising government spending and falling revenue collection due to the COVID-19 crisis. Like the RBA, we remain of the view that inflation will likely remain subdued in the next year or two. In a low interest rate environment this outcome would likely continue to be supportive of long duration growth stocks, including many of the technology names we have exposure in the portfolio.

Confronted with a uncertain global macro backdrop and a 'lower for longer' interest rate outlook, we have strategically positioned our portfolio towards beneficiaries of the structural trends which are accelerating in a COVID-19 impacted world, such as data usage, cloud computing and the acceleration of digitalisation and e-commerce. We are actively positioning the portfolio away from the most heavily disrupted sectors such as old-world media, bricks and mortar retailers and REITS. We are looking for resilient and innovative structural winners, who can control their own destiny and who can continue exploiting their competitive advantage, taking share from lower-tech incumbents, and growing independently of the economic cycle. Portfolio holdings such as NEXTDC and Kogan.com Limited currently fit this profile.

One of the more common questions we get asked lately is "are we concerned about the results in the upcoming reporting season given the economic uncertainty"? On the contrary, we have rarely had more transparency on our portfolio holdings heading into a results period given the elevated levels of communication by companies with the investment community over recent weeks and months. Many of the Fund's holdings have recently provided trading updates to the market meaning that the FY20 results are largely known, which is a pleasant change to most years. Where there remains meaningful uncertainty or opaqueness, either on recent trading or on balance sheet strength or cash collection, we have tended to exit those holdings ahead of the August reporting season. We therefore do not expect too many earnings surprising in the August reporting season.

Obviously, we will be focusing on outlook for the companies in our investment universe when they report as there remains a host of unknowns which makes it a tricky time to be an investor. Questions such as when a vaccine will be found or when the COVID-19 infection rate will moderate across the globe are simply unknown. This makes investing with conviction somewhat challenging right now. We therefore have a portfolio of stocks with business models that ought to survive any eventuality including balance sheets that can survive a protracted economic downturn.

It has been a busy start to the new year for the investment team bunkered down in Melbourne with COVID-19 restrictions. We are working diligently to help ensure strong investment outcomes for our clients (and ourselves as Fund investors) and we have enjoyed a promising start to the August reporting period, albeit it is early days. We continue to wish our readers and their loved one's good health in these challenging times and look forward to updating you again in September on the August results.

Top 5 holdings#

Company	ASX code
Appen Limited	APX
Bapcor Limited	BAP
Kogan.com Ltd	KGN
Nextdc Limited	NXT
Steadfast Group Ltd	SDF

The top 5 portfolio holdings are in alphabetical order and may not be representative of current or future investments.

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[†]The total return performance figures quoted are historical, calculated using hard-close end-of-month mid-prices and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. The performance is quoted net of all fees and expenses. The index does not incur these costs. This information is provided for general comparative purposes.
[*] The performance comparison of $100,000 over 10 years is for illustrative purposes only. All returns shown are based on Australian dollar figures. Past performance is not a reliable indicator of future performance. The total returns shown are prepared on an ongoing basis (i.e. they include all ongoing fees and expenses and assume reinvestment of all distributions). They do not take personal taxation into account. The comparison with the S&P/ASX Small Ordinaries Accumulation Index is for comparative purposes only. Index returns do not allow for transactional, management, operational or tax costs. An index is not managed and investors cannot invest directly in an index.