

# OC Funds Management celebrates 20 years of investing in Australian small companies



(L-R) Robert Calnon, Robert Frost, Stephen Evans, Daniel Stein

In 2020 OC Funds Management (OC) in partnership with Copia achieved a milestone that is quite rare among its Australian small cap investment peers. In December OC reaches its 20-year anniversary of investing in Australian small companies and micro-caps (small caps). And just like the small gems it seeks to discover that will grow to become larger successful enterprises, OC has grown from humble beginnings to become one of Australia’s longest-running small cap boutiques with \$1.3 billion under management, three funds with Lonsec Highly Recommended ratings, an outstanding track record of outperformance for each of its funds since inception, as well as several fund manager of the year accolades.

OC opened its doors in December 2000 and launched its flagship OC Premium Small Companies

Fund. Each dollar invested in this strategy at inception has grown to \$7.38 in today’s terms, representing an average return of over 11 per cent every year for 20 years. By comparison, a passive investment would have yielded just \$2.34.

Like most fund managers of its vintage, OC’s journey over twenty years hasn’t always been smooth sailing with the investment team weathering a number of stock market crises over the years including the Global Financial Crisis in 2007-08 and the fall-out from September 11 in 2001-02.

Each crisis has brought a new set of opportunities and the COVID-19 pandemic this year was no different with the funds performing strongly following the initial market shock.

## Build wealth with a safe pair of hands

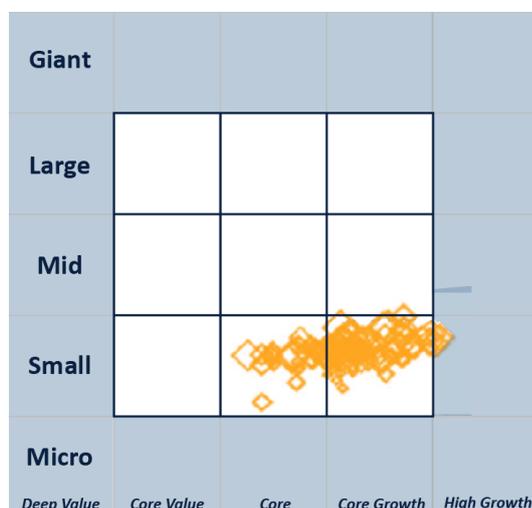
OC’s objective as a small caps fund manager is to build wealth for clients and to provide a safe pair of hands. Providing a degree of safety is nuanced for OC as the small cap sector offers some of the most exciting investment opportunities in the Australian sharemarket, but at the same time the sector can exhibit periodic volatility and speculative excesses which can often end badly for unsophisticated investors. These properties need to be navigated by a well-resourced, stable and thorough investment team with an eye for capital preservation and a proven ability to back long-term winners.

OC’s investment strategy has remained consistent through the years, focusing on high-quality and sustainable businesses, supported by quality management teams, attractive investment fundamentals and reasonable valuations.

The chart below shows how the OC Premium Small Companies Fund has been true-to-label in its exposure to small caps and a ‘core’ investment style with a bias towards ‘growth’, but also willingness to back ‘value’ where opportunity arises.

### OC Premium Small Companies Fund Style bias and market cap exposure

August 2004 to September 2020



Source: Morningstar

## Stock stories

One of the most exciting attributes of investing in small caps is the opportunity to back companies early before they are well known and widely researched. There are many examples of stocks that OC identified and backed early that have gone on to become household names. Equally, there are stocks that OC had the opportunity to invest in but held back, as well as some lessons from stocks that didn’t work out as planned.

100

Stocks now in the top 100



Stocks on their growth journey

OC was an early investor in digital disruptors that have progressed up the market capitalisation pathway, including REA Group, Carsales.com Limited and Seek Limited.



Stocks that were avoided

Passing on poor investments is a skill in itself and OC has avoided its share of ‘blow-ups’ over the years, two recent examples being Isignthis Ltd and Big Un Limited.



Lessons learnt

OC invested in Slater & Gordon which was an outstanding growth story until management expanded offshore. The key learning was for the team to be wary of fast tracked, large scale offshore acquisitions that likely stretch even the strongest of management teams beyond their capabilities.

## Investing in small caps can still be defensive

It is understandable to think that investing in small caps must be risky, but there are measures a fund manager can employ to reduce the risk of capital loss to the investor.

OC’s mantra of being a safe pair of hands reflects its high aversion to risk and focus on company fundamentals as the first layer of defense. The team will only invest in a company once the risks are clearly understood, and the stock is trading below its intrinsic value (with a reasonable margin of safety).

Capital preservation is a very important part of OC’s investment approach as evidenced by the relative outperformance when the market is falling, compared to rising since inception.

## Investing also about people

According to OC Funds Management Head of Investments Rob Frost, the ability to maintain stability in the four person investment team has been a critical ingredient in the success and longevity of the business.

The two senior members of the team, Rob Calnon (Senior Investment Analyst/Dealer) and Stephen Evans (Senior Investment Analyst), have been with OC and worked directly with Frost for 14 and 10 years respectively.

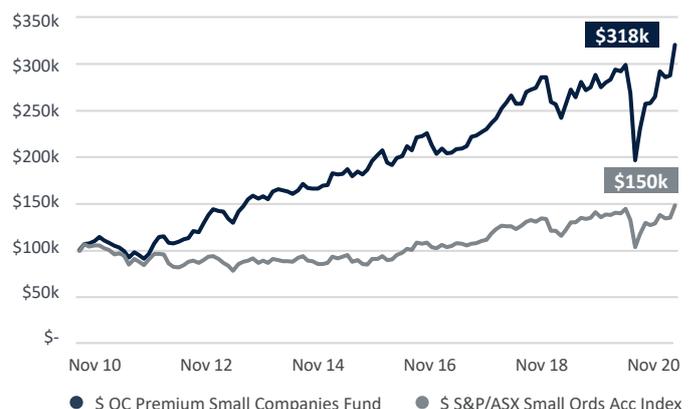
The most recent addition, Daniel Stein (Analyst), joined in 2017. There has been no turnover in the investment team in well over a decade. The team dynamics work wonderfully with a broad range of skill-sets interplaying to create a strong team, aligned with investors through equity ownership and investments in the funds themselves. Few fund managers, particularly in the small caps space, can match this level of experience, tenure and stability.

## Three tips to longevity

Success as a fund manager requires a number of ingredients to work together, evidenced by the ability to perform and create wealth for investors over a long period of time. For OC, the following behaviours and cultural attributes have underpinned the longevity and success of the business.

- 1 Be passionate about the stock market. Be naturally engaged in what you do for a living and intellectually curious about it. This should give you a solid head start over someone for whom investing is merely a means to an end.
- 2 Build strong networks and access to information from a broad range of sources. This may include contacts in the unlisted space to cross check assumptions, or even relationships with management well beyond the CEO and CFO of companies.
- 3 Be open to admit you can get it wrong and cut losses at the appropriate times. Humans are not inherently good at admitting to mistakes but an inability to take a loss, when it is otherwise the rational thing to do, can be very costly.

## Performance comparison of \$100,000 over 10 years\*



## What researchers say

OC has been rated by both Lonsec and Zenith since the early 2000's and the comments below are extracted from the most recent rating reports of the OC Premium Small Companies Fund in 2020.



### Lonsec – Highly Recommended

*“Stable and highly-regarded investment team with significant co-tenure and experience. Key team members have material co-investment and equity ownership.”*



### Zenith - Recommended

*“Zenith considers the Fund’s investment team to be well resourced and experienced for the management of Australian small and micro-cap strategies.”*

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\*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.

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