December 2019 Monthly Report plus 2019 Year in Review

Returns 31-Dec-12 to 31-Dec-19

	Norse Capital	All Ords Accum	Outperformance	Small Ords Accum	Outperformance
Inception	251.95%	95.98%	155.96%	58.32%	193.63%
Inception per annum	19.68%	10.09%	9.60%	6.78%	12.90%
CY2019	43.44%	24.06%	19.38%	21.36%	22.08%
CY2018	7.46%	-3.53%	10.99%	-8.67%	16.13%
CY2017	15.55%	12.47%	3.08%	20.02%	-4.46%
CY2016	9.31%	11.65%	-2.33%	13.18%	-3.87%
CY2015	36.80%	3.78%	33.02%	10.16%	26.65%
CY2014	10.81%	5.02%	5.79%	-3.81%	14.62%
CY2013	19.24%	19.66%	-0.41%	-0.76%	20.00%
1m	-2.91%	-1.90%	-1.01%	-0.29%	-2.62%
3m	2.34%	0.75%	1.59%	0.76%	1.58%
6m	1.17%	3.59%	-2.42%	3.89%	-2.72%
1y	43.44%	24.06%	19.38%	21.36%	22.08%
2y pa	24.15%	9.40%	14.76%	5.28%	18.87%
3y pa	21.20%	10.40%	10.79%	9.97%	11.23%
5y pa	21.63%	9.29%	12.34%	10.64%	10.99%
7y pa	19.68%	10.09%	9.60%	6.78%	12.90%
Sharpe Ratio	1.44	0.78	1.85x	0.43	3.38x
Sortino Ratio	2.92	1.24	2.35x	0.65	4.47x
Annualised standard deviation	11.75%	10.73%		12.95%	
Highest monthly return	11.78%	7.00%		9.81%	
Largest monthly loss	-5.82%	-7.30%		-9.60%	
Largest drawdown	-10.28%	-12.23%		-17.69%	
% positive months	72.62%	64.29%		57.14%	

Happy new year to you and yours and best wishes for a healthy and prosperous new decade.

A little bit of a later release date for the monthly report over the holiday season. We'll give a short recap on December's performance then take a more in-depth look at 2019's performance.

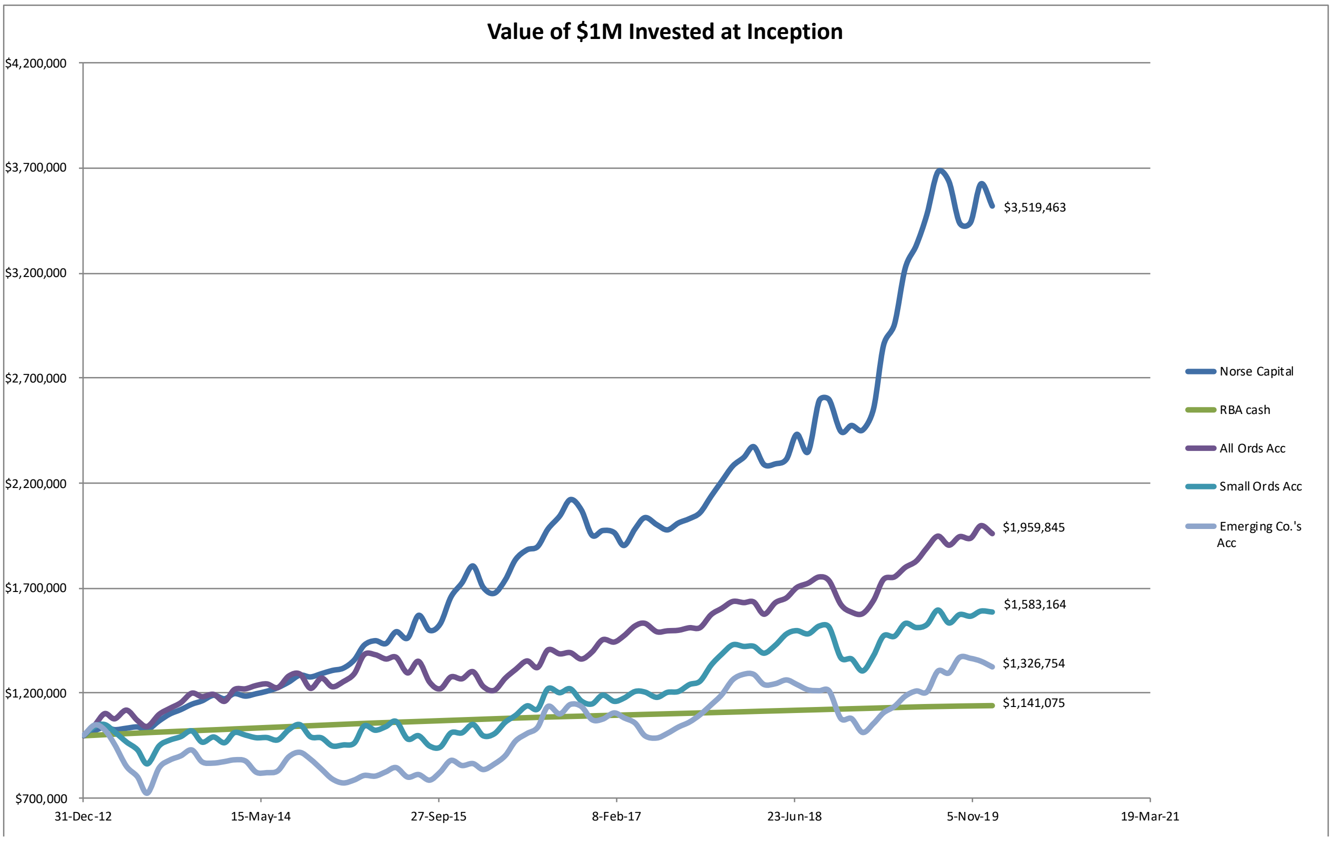
A negative month for the portfolio down -2.91%, a bit worse than the All Ords (down 1.90%) and worse than the Small Ords (down 0.29%) and quite a bit behind both the S&P500 (up 2.9%) and the Nasdaq (up 3.5%).

The one positive performance of note in December came from AAPL, up +9.9%, setting new all-time highs. Notable losers on the month were APX, down 8.3% and PME down 9.6%. Our US-listed enterprise software basket cost the portfolio -0.95% while the AUD moving above 70c cost the portfolio another -0.7%.

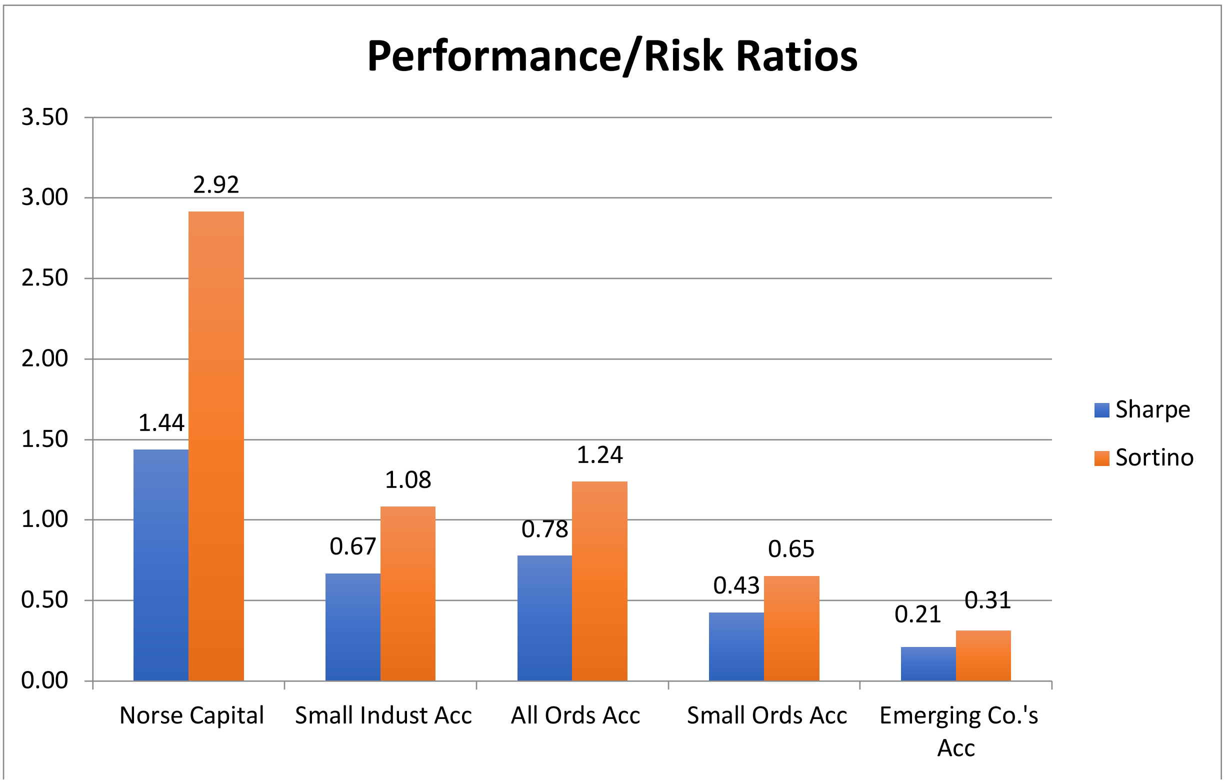
<u>Portfolio Holdings:</u>

Cash:	25.8% (AUD and USD)
Non-AUD exposure:	20.2%
Longs:	73.3%
Shorts:	-6.3%
Options delta:	+2.8%
Net exposure:	69.8%
Top 5 equities (alphabetical):	AAPL, APX, EML, PME, RMD

We have renamed "Hedge delta" to "Options delta" in the statistics above as the delta includes long call options which have replaced outright stocks in our enterprise software basket as well as the short delta from our index and other hedges. Our outright net exposure remains relatively similar to last month's at just under 70% long.



Value of $1M Invested at Inception
$4,200,000
$3,700,000
$3,200,000
$2,700,000
$2,200,000
$1,700,000
$1,200,000
$700,000
31-Dec-12
15-May-14
27-Sep-15
8-Feb-17
23-Jun-18
5-Nov-19
19-Mar-21
$3,519,463
$1,959,845
$1,583,164
$1,326,754
$1,141,075
Norse Capital
RBA cash
All Ords Acc
Small Ords Acc
Emerging Co.'s Acc



Performance/Risk Ratios
3.50
3.00
2.50
2.00
1.50
1.00
0.50
0.00
1.44
2.92
0.67
1.08
0.78
1.24
0.43
0.65
0.21
0.31
Norse Capital
Small Indust Acc
All Ords Acc
Small Ords Acc
Emerging Co.'s Acc
Sharpe
Sortino

2019 Year in Review

The change of the calendar to 2020 marks the seven year point for our portfolio; aside from adding another row to our returns table (for 7 year performance) it is also a milestone that looked far in the distance way back at inception and serves to remind us that investing is a long-term effort. Needless to say, it is pleasing to have made it thus far. 2019 also has locked in the best annual equity index performances in the markets we follow during that same seven year period, with double digit performances from indices in Australia and the US. The All Ords tacked on +24.06% and the Small Ords +21.36% on a total return basis while in the US the S&P500 was up +28.9% and the Nasdaq up +35.2%. Against that backdrop our portfolio also managed to put in its best calendar year performance to date, up +43.44%.

We are obviously more than happy with 2019's result and will bank CY2019 in our performance statistics. We do have to recognise the quirk of timing where there was a substantial fall in markets towards the end of 2018 which sowed the seeds for 2019's outperformance, creating the highest return for indices and our portfolio following CY2018's lowest performance (again for the last 7 years). All that shows is that changing starting and ending points can play with statistics and why it is important to look at results and invest over the long term as we will continue to do.

As previously, we will attempt to glean some learnings if possible from 2019 to where we ended up with our +43.44% result. From a high level view, we started the year with a cash weighting of 33.9% and a net exposure of 55.5%, reflecting the positive gamma of our hedges at the low point of 2018's end of year correction. Our exposure steadily increased during the year as a function of both the portfolio's positive gamma in rising markets and good performance from our holdings to end with a weighting of 69.8%, (averaging just under 62%). In such a high-performing year (and with 20/20 hindsight), we would obviously have been better off not hedging at all and should have been 100% invested. However we have yet to receive a replacement crystal ball since returning the original to amazon.com via their returns process. Until then, we will continue to maintain a decent cash weighting and a hedge component to the portfolio as we have done since inception.

To keep this report concise and given 2019's performance and the number of contributors towards that performance, this report on 2019 will comment on individual contributors that have had a greater than +/-4%

effect on the year's performance (vs previous years' commentaries using a +/-1% threshold). We'll start with the detractors:

<u>Detractors (> 4.0% loss to performance):</u>

Shorts and hedges: -7.3%
Not surprisingly for the best year for equity indices in our observation period, the biggest detractor for 2019 came from our shorts and hedges. Partly a function of giving back end of 2018 gains/profits in our hedge portfolio near the depths of the market correction where implied volatility was particularly high and also a function of a strong market eroding the value of our long put options which we continued to buy in a rising market. That combined with instituting more direct shorts at the beginning of the year has resulted in our biggest annual detraction from performance. Moreover, in the second half of 2019, the market "rotation" we have mentioned in our monthly missives served as a double whammy whereby our hedges not only failed to mitigate drops in our holdings but added to losses.

Honourable mention on the detractors front and given my penchant for ruminating over "if only's", goes to an act of commission that sold a stock I previously blogged about on the website that could otherwise have been a big contributor. We sold out of AVH in late 2018 following FDA approval of their burns device (roughly doubling our investment), only for the stock to subsequently more than 6-bag in 2019. You can't win them all - the initial thesis was predicated (correctly) on a clear path to imminent FDA approval which the market seemed to have too severely discounted. Given the thesis was fulfilled, I closed the position. Perhaps one learning would be to have kept tabs on the business (especially given the knowledge gleaned from researching the company) instead of removing it entirely from the watch list as the price increased to salve my ego. Sigh, if only…

<u>Contributors (> 4.0% contribution to performance):</u>

APX +10.7%
Following on from APX contributing +6.1% to the portfolio in 2018, the shares rose over +75% in 2019 to contribute another +10.7% to the portfolio in 2019. A big year for Appen with the acquisition of Figure 8 in the US (along with an associated capital raise) to give the company increased capabilities in the automation of data annotation. Despite the expected upfront drag from this acquisition Appen continued its positive financial performance, guiding for EBITDA growth around ~+40% for its

calendar year end results. The stock price also had a big year with an initial rush up to highs at $32 before falling back below $20 with initial concerns over the performance of the Figure 8 acquisition. We did trim our position during the year at an average price slightly higher than the year-end price due to portfolio weighting considerations which helped on the way back down. However Appen still remains our largest holding at just over 12% of the portfolio and given we think we are still in the early stages of the AI/data tailwinds, we intend to continue to allow our holding to compound over time while holding through volatile periods, as we saw in 2019.

PME +10.3%

Pro Medicus contributed another +10.3% towards our portfolio's performance following on from the previous year's +1.8% contribution, with the shares up over +105% in 2019, reaching a high over $38 before ending the year at $22.35. The share price volatility a function of the company continuing to perform well, with profit up over +91% while continuing to win new deals in the US, further upside with the shares admitted to the ASX200, counterbalanced by director sales near the year's highs with the shares on a lofty multiple. 2019 saw our first ever sales of PME as we reduced our position on the order of ~45% at an average price near $30 due to portfolio weighting decisions and as the share price had seemed to have gotten ahead of itself. PME remains a top holding (now in 3rd place) at just under 7% of the portfolio. One of, if not the top quality stocks on the ASX with a long runway ahead, we intend to maintain a position in PME for the foreseeable future.

EML +5.5%

A portfolio holding since early 2018, to which we have added as the business has performed, EML contributed +5.5% performance to 2019's results as the shares soared almost 205% on the year. The payments business continued to perform well with EBITDA up +40% to post an impressive 5y EBITDA CAGR of +82% with leadership in several verticals. This was compounded by the large acquisition of PFS which promises to give scale and adds digital banking as a service and multi-currency capabilities, along with winning the gift card business of the largest US mall operator, culminating in EML being added to the ASX200 late in 2019. EML is now our 2nd largest holding.

US-listed enterprise software basket +4.6%

We started building our basket of US-listed enterprise software companies in mid to late 2018, allocating on the order of 5% of the portfolio through early 2019. Today the basket represents over 11.5% of the portfolio or would otherwise be our 2nd largest holding if counted as one stock. We have previously mentioned the 2 largest holdings in our basket, AYX and TTD which together make up just under half the basket weighting. The stocks were up over 68% and 123% respectively and epitomise (along with the other holdings in our basket) the types of exposure we are keen to have to the burgeoning cloud/enterprise software space and the tremendous growth opportunities therein.

AAPL +4.3%
After a negative share price performance in 2018 where the shares dropped -6.8% (and out of our top 5 holdings), AAPL rebounded +86.2% for 2019 to add +4.3% to the portfolio (and rejoin the top 5). Truly incredible for a US trillion dollar market cap company. The share price performance in one sense shows the effect of the start of the period coinciding with a nadir in AAPL shares after the company downgraded quarterly results and their outlook early in 2019 on the back of reduced demand in China. Counter to that though, the share price has since soared to new all-time highs as the business has demonstrated strength outside of its traditional hardware iPhone business and into services and wearables which have shown strong growth and now represent on the order of 20% of AAPL's business.

Honourable mentions for positive performance to NAN, EVS, RMD, and VHT with each adding just above and below +2% to 2019's performance.

So what lessons can we take from 2019?

At the risk of repeating previous annual commentaries, the "easy" answer is to try to continue to allow our holdings to compound and grow sizably over time which is what we have done with just about all our biggest contributors. (A counter example that highlights this is where we finally bought back a position in ALU in 2019 at more than double where we'd last sold out, when we should have kept some of the holdings instead of trying to finesse entry and exit points). Easy in theory, not so easy in practice in the face of substantial volatility as we saw in 2019. Some mitigation was provided by selling a portion of some of our holdings for portfolio weighting considerations which proved valid in hindsight (so far at least). More a personal comfort decision at what point a position becomes too large. For us it was APX approaching 25% and PME approaching 15% coupled with our assessment of their share prices at the time.

No real significant losses in 2019 from individual stock positions but definitely a significant loss from shorts and hedging. A tough year on the hedging front, to be expected in a very good performance year for equity markets. Perhaps we should have been more proactive in taking temporary profits on hedge positions but psychologically difficult to do in the depths of corrections when balanced against the risk of further declines. For outright shorts, we probably need to maintain a tighter leash on positions.

Finally, we look forward to the new decade starting in 2020. We remain optimistic about our current holdings and our process of discovering new compounders going forwards. We do remain cognisant of the tremendous year that was for equity markets which has brought some returns forward and consequently set the bar higher for future returns. We have little (no?) ability to forecast what will happen in the short-term and so will remain focused on the long-term potential of our existing and to-be-added holdings.

All the best for the new year and decade.