Asia Small Companies Unit Class
TAMIM Fund

At 31 July 2020

The past month has seen a 65% increase in the official number of Covid-19 cases globally, a marginal deceleration from the 69% monthly growth rate recorded in June. Asian equity markets for small to mid-sized stocks was mixed during July ending the month up 1.5% in USD terms. The continued recovery in Asia markets was again offset by strength in the Australian currency, rising 3.7% versus the US dollar during June which resulted in a 2.2% decline in the regional equity index in Australian dollar terms. During the year to date Asian small to mid-sized companies have fallen by 6.9% in US dollar terms and declined by 8.3% in Australian dollar terms.

For a second successive month the Greater China markets recorded strong performance in July in USD terms with China increasing 11.1% followed by Taiwan up 5.7% and Hong Kong up 1.9%. Taiwan ended the period at a new all-time high, a mark that has stood for three decades. Taiwan has managed to quietly manoeuvre around the global trade tensions and taken the opportunity to move some production capacity back to the domestic economy and away from China helping to boost local incomes. China managed a second month of double digit percentage gain despite ongoing tension with the United States, massive flooding and a border dispute with India. The Trump administration has continued their strategy of blaming China for the Covid-19 pandemic and raised the diplomatic stakes in July by forcing China to close their consulate in Houston. China responded by ordering shut the United States consulate in the southwestern city of Chengdu, a place that is better known for excellent spicy cuisine instead of geopolitical retaliation.

Elsewhere in the region Korea and Singapore recorded gains of 10.6% and 2.3% respectively while Japan declined by 3.2%. The decline in Japan was largely in reaction to an acceleration in the number of Covid-19 cases which increased by 88% during July while the number of deaths passed 1,000 to end the month at 1,011. These Covid-19 numbers have dampened sentiment domestically although it should be noted that international investors were net buyers throughout the month of July. Towards the end of July Japanese companies started reporting first quarter results.

Public broadcaster NHK reported that Japan's government have decided to begin discussions over easing immigration restrictions with China, South Korea and Taiwan. Increased immigration is the key to solving Japan's demographic imbalance and declining population. In recent years Japan has adopted informal measures to increase immigration without any change to the very restrictive formal stance. We have now seen the first signs of a public policy directed at solving the declining population in Japan. We view this as a positive step.

As long-term investors we do not typically execute short-term transactions. We made an exception with BayCurrent Consulting a business management and IT consulting business in Japan that we added to the portfolio on 8th July and sold three weeks later for a profit of 49%. BayCurrent Consulting did announce a strong set of quarterly results, however, following the 49% increase in share price during month that pushed the price/earnings ratio to a level in excess of 30x we were happy to walk away with a nice profit. Two more companies in the portfolio increased by more than 40% during July, China Lesso Group jumped 48.4% and United Microelectronics Corp (UMC) by 40.6%. Plastic pipe maker China Lesso Group is a long-term holding in our portfolio and a beneficiary of ongoing urbanisation in China, the shares trade on a forward price/earnings ratio of 10.6x. Taiwanese semiconductor foundry business UMC was added to the portfolio in May and the company surprised the market in July with results more than 50% above consensus expectations of the 20 analysts covering the stock. UMC trades on a forward price/earnings ratio of 13.8x and a yield of 6%. The weakest stock in the portfolio was house builder Open House which fell by 18.9%, having previously increased by 66% in the prior quarter. Open House trades on a price/earnings ratio of 6.8x and we are maintaining our position.

We will continue to invest in Asian small to mid-sized companies with strong value, momentum and quality attributes together with accounting, strategy and governance standards that meet our requirements. Long-term returns will be generated by the ability of our companies to deliver growing profits and dividends.

Stock Review

United Microelectronics Corporation (UMC) manufactures and markets integrated circuits. The company provides wafer manufacturing, assembly, testing, mask production and design services. UMC operates 12 fabs that are located throughout Asia with a maximum capacity of more than 750,000 8-inch equivalent wafers per month. The company employs approximately 19,000 people worldwide, with offices in Taiwan, China, United States, Europe, Japan, Korea and Singapore. In Q3 2019, UMC ranked fourth in the pure foundry industry with 6.7% market share (source: Trend Force). UMC manufactures semiconductors using advanced production processes for customers based on its own proprietary integrated circuit designs. UMC's wafer fabrication process include services such as design, mask making, testing, and assembly services.

Accounting, Strategy and Governance Comments

Accounting

UMC has been audited by Ernst & Young since the year 2000, the engagement of a big name accounting firm is a positive.

With the listing of ADRs in the United States, UMC is subject to oversight from the Securities and Exchange Commission. There have been no financial restatements or revisions since 2015. UMC had one critical audit matter in their 20-F filing in April 2020 relating to the valuation of slow moving inventories, we are satisfied that the company has addressed this issue.

UMC has generally kept its debt levels ranging from 21% to 33.6% of assets between 2015 to 2019, very low by the standard of the industry. UMC moved into a net cash position in 2019 and currently holds NTD 36.8 billion (equivalent to USD 1.25 billion).

Strategy

Since the semiconductor industry is highly cyclical, UMC is exposed to periods of rapid expansion and contraction. Other factors that affect UMC sales are the worldwide demand for semiconductor products, pricing, worldwide production capacity, capacity utilization, technology migration and fluctuations in foreign currency exchange rates. UMC's sales growth has expanded in the last five years by a CAGR of just 1.1%, while net profit declined at a CAGR of 2.7% during the period. However, we note that despite the slow historic backdrop for sales growth, net profit grew by 26.4% in 2019 and in the most recent figures for the six months to end June 2020 sales increased by 26.3% versus the equivalent period in 2019.

UMC has a well diversified spread of customers. Asia Ex-Japan accounted for 55% of Q2 2020 revenue, North America 31%, Europe 5% and Japan 9%. Among UMC's customers are Xilinx, Broadcom, MediaTek, Realtek, and Novatek, Texas Instruments, Intel Mobile and STMicroelectronics.

We believe UMC will transform into a specialty foundry changing its business model and focus on 28nm, 40nm and 8" foundry products, which will result in significantly improved profitability by reducing capex and R&D. UMC is currently focusing on the production efficiency of its legacy nodes (above 28nm process) given the strong competition in the advanced nodes (less than 28nm process). Hence, it has been able to expand its wafer output capacity by 5%-6% annually from 2016 to 2019, while posting lower capex every year during this period.

Gross margin is likely to continue expanding into H2 and 2021, as 28nm helps the overall cost structure, and as depreciation expenses come off with lower capex. We expect UMC to reduce capex to US$800m vs. guidance of US$1bn for 2020.

Governance

UMC publishes their corporate governance policy (most recently March 2019) and maintains the standards required in Taiwan Stock Exchange Listing Rules. The Board comprises nine Directors or which four are independent. Directors serve terms of three years and can stand for re-election.

UMC has been ordered to pay a fine of NTD 100m (equivalent to USD 3.5m) by a district court in Taichung City which found the company and three of its employees guilty in a trade secret theft case brought by U.S.-based memory chipmaker Micron Technology. UMC has denied its DRAM technology is related to that of Micron. Technology disputes of this type are "normal" in this industry and we don't consider this to be a significant lapse in UMC's governance. UMC faces a bigger challenge with respect to the legal action taking place in the United States courts associated with its collaboration with Fujian Jinhua.

During the past five years, total dividend pay-out has averaged 75.6%, we expect the high payout ratio to be maintained.

Value, Momentum and Quality Comments

UMC has an overall VMQ score in the top 30% of our universe of companies with an especially strong score for value driven by the dividend yield in excess of 6% and price/book ratio of 1.0.

UMC's return on equity is improving towards the 10% plus level, having been as low as 3% five years ago. This improving trend for return on equity will help the score for quality, together with the strong balance sheet with net cash.

There are 20 analysts providing coverage of UMC, the second quarter results came as a complete surprise to the analyst community, beating their estimates by more than 50%. Net income for the six months ending 30 June 2020 increased from TWD 1,035m to 7,281m resulting in an eps uplift from TWD 0.25 to 0.74 for period. The positive surprise contained in those second quarter results has generated a significant uplift in earnings forecasts for 2020 and 2021 and underpins a strong and improving score for momentum in our VMQ analysis.

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Fund Overview

The TAMIM Fund Asia Small Companies unit class seeks to achieve a high real rate of return over the long-term within defined risk parameters acceptable to the Investment Manager through a diversified portfolio of Asian small and mid-cap shares.

Key Facts

Investment Structure:	Unlisted unit trust
Minimum investment:	A$100,000
Applications:	Processed monthly
Redemptions:	Monthly, with 30 days notice
Unit pricing frequency:	Monthly
Distribution frequency:	Annually
Management fee:	1.00% p.a.
Expense recovery fee:	Up to 0.35%
Performance fee:	20% of performance in excess of hurdle
Hurdle:	MSCI AC Asia Small & Mid Cap Index
Buy/Sell Spread:	+0.30%/-0.30%
Exit fee:	Nil
Single security limit:	+/- 5% relative to Benchmark
Country/Sector limit:	+/- 10% relative to Benchmark
Target number of holdings:	60-80
Portfolio turnover:	< 30-40% p.a.
Investable universe:	MSCI AC Asia Small & Mid Cap (US$ 500m - 10bn)
Cash level (typical):	0-100% (0-5%)

Returns

	1m	3m	6m	1y	Since inception p.a.
TAMIM Asia Small Comp.	-0.81%	-0.07%	-7.73%	0.54%	-2.27%
MSCI AC Asia SMID	-2.55%	-0.27%	-9.63%	-3.06%	-2.97%

Note: Returns are quoted net of fees and assume distributions are reinvested. Past performance is no guarantee of future performance. MSCI AC Asia SMID refers to the MSCI AC Asia Small & Mid Cap Index in AUD. Inception 1 October 2018.

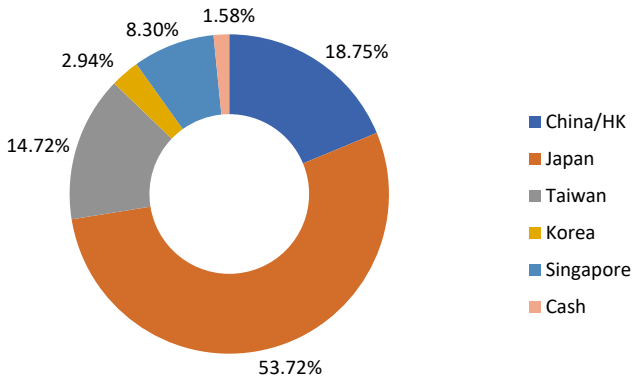
NAV

	Buy Price	Mid Price	Redemption Price
AU$	$7.6941	$7.6711	$7.6481

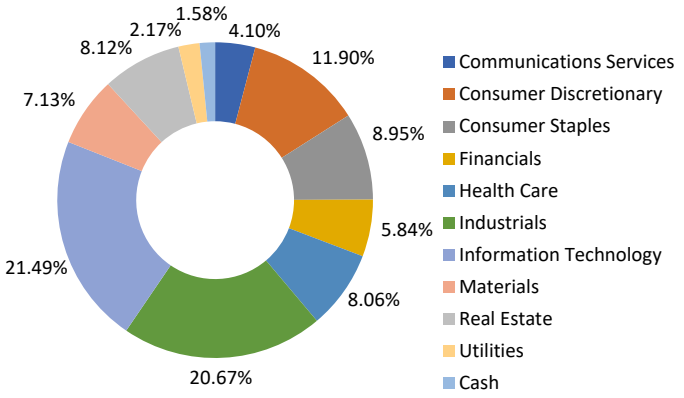
Portfolio Profile

Equity	98.42%
Cash	1.58%

Regional Allocation



Sector Allocation



Selection of 5 Holdings

Stock	Code	Country
Open House Co. Ltd.	3288.T	Japan
Sheng Siong Group Ltd	OV8.SI	Singapore
Simplo Technology Co. Ltd	6121.TWO	Taiwan
China Lesso Group Holdings Ltd.	2128.HK	China/HK
SFA Engineering Corp.	056190.KS	South Korea