DMX
ASSET MANAGEMENT

DMX Australian Shares Fund
Investing in the most compelling Australian smaller company opportunities

DMX Australian Shares Fund
June 2021 – Investor Update

A wholesale unit trust managed by:
DMX Asset Management Limited
AFSL 459 120
13/111 Elizabeth Street, Sydney, NSW 2000
Trustee & Administrator:
Fundhost Limited AFSL 233 045

Unit price (mid) based on NAV (31 May 2021)	**$1.0401**
Unit price (mid) based on NAV (30 June 2021)	**$1.0651**
Number of Stocks	37
% cash held - month end	8%

1-month return	2.40%
3-month return	6.29%
Since inception (1 March 2021)	6.51%
Fund size (gross assets)	$6m

Dear Investor,

DMXASF's NAV increased 2.40% (after fees and expenses) in line with the ASX 200 Total Return Index's 2.26% gain. We've covered a lot of ground in the first four months of this new fund and we now own 37 diverse positions (very near our 40 maximum) and cash is down to 8%. Of our 92% invested, approximately 65% is invested across 27 positions also held by DMX Capital Partners (DMXCP) while 27% is invested across 10 additional companies. The average market capitalisation of the overlapping 27 stocks is ~$100m, while the 10 additional names are almost all within the $100-500m market capitalisation range, with an average of value ~$350m.

Portfolio Commentary

The Fund rose 2.4% for the month, in-line with the broader market, and driven by continued advances from **Cryosite** (+14%) and **Laserbond** (+11%) as well as gains in **Readytech** (+16%) and a partial recovery to some of our other technology-focused names including **CV Check**, **Raiz**, and **Knosys** (up 12%, 16% and 8% respectively). Some of these companies, we believe, have seen their share prices fall following capital raises at higher prices in recent months together with some potential tax-loss selling heading into 30 June. We've taken advantage of weakness by selectively adding, in particular where we had previously only established partial-positions during our implementation phase.

On the other side of the ledger, losses were recorded with retailers **Shaver Shop** (-7%) and **Dusk** (-5%) though these were mitigated by a 6% gain for larger-position-sized **Michael Hill** which we discuss in more detail below.

Newsflow included positive updates from a number of holdings including:

- **CV Check**, an online verification company reported record revenues for the month of May putting them on a revenue run-rate $26.4m. This is up from a proforma June 20 run-rate of $17.3m. Impressively, this growth is being achieved while being cashflow positive. Integration of their recent software acquisition is on-track, and we look forward to a strong FY22 after a weak FY21 due to COVID. CV Check is a growing, cashflow-positive, and very interesting technology-driven business with substantial operations across Australia & New Zealand, and the potential to grow meaningfully into international markets.

- **Joyce Corporation**, an investment company that owns two growing national businesses, KWB Kitchens and Bedshed provided a store roll-out update. Both KWB and Bedshed are expanding into the key NSW market. KWB is planning to open four new showrooms per annum providing a strong runway for growth. While no financials were given, management highlighted 2H revenues would be consistent with their 1H which saw

16% revenue growth on PCP. Joyce is also likely to provide a strong dividend of around 14c for FY21. At DMX we have been long-time investors in Joyce Corporation and see significant underlying value within its two subsidiaries, and in particular KWB. Some reinvestment risk does exist with this business, and our preference would be for the company to be strategically focused on maximising value from its two valuable businesses rather than seeking to grow into new verticals.

- **Michael Hill**, a jewellery retailer with a substantial store network across Australia, New Zealand and Canada, announced some internal shifts/promotions within its Board and senior management. Emma Hill, who has been on the board since 2007 and Chair since 2015, is remaining a director but handing the Chair over to fellow long-time director (and former Air NZ CEO) Rob Fyfe. At the same time, CEO Daniel Bracken is being promoted to the Board, becoming Managing Director. We view these subtle shifts as positive in supporting the culture within the business and recognising and harnessing the talents and capabilities within the organisation.

- **PTB Group**, a global aircraft engine maintenance company, announced the acquisition of assets and customers of United Turbine's PT6 engine overhaul division. We understand this opens up access to Caribbean aircraft operators which provides similar characteristics as the successful Pacific operations out of Brisbane. We see this acquisition as positive and is consistent with objectives discussed previously with management. Important niche 'services' businesses like PTB are highly interesting to us as they often have dominant market shares in certain geographies, benefit from scale, are a small but critical part of the ongoing operation of often important equipment (none more important than aircraft engines!), and are supported (in particular in aviation) by cumbersome regulatory frameworks which keep upstarts at bay.

- **Sequoia**, which is a financial services firm providing various services directly to clients, as well as a range of business support and compliance services to accountants, financial planners and third party AFSL holders, continued its strong earnings momentum with another FY21 upgrade. EBITDA is forecast to more than double from $4.8m in FY20 to $11m in FY21 on revenue growth of around 35%. This has been driven by increased scale from recent acquisitions and, we understand, the successful cross-sell of services. Sequoia has demonstrated strong capability in both organically growing their core business and identifying, acquiring and integrating value-adding businesses to the group. Its market price has been following developments over time *directionally*, but we believe has some way to go to fully reflect the quality of the business.

Thinking about Performance Attribution

The DMXCP monthly report includes a detailed full-year performance breakdown highlighting a large range of companies that contributed positively (and a few that detracted) for the year. At just the 4-month mark a similar analysis wouldn't yet be useful for the DMXASF. But we encourage DMXASF investors and prospective investors to review the DMXCP report to glean useful insights into our firm's investment philosophy and process. A key insight for us in reviewing the DMXCP performance (both of the past year and really since its inception in 2015) is that strong returns can be achieved while running a well-diversified portfolio. Being overly concentrated carries two forms of excessive stock-selection risk: (1) you risk picking the wrong stocks (mistakes and adverse developments are par for the course in assessing companies and investing); and (2) you risk missing out on the positive surprises (and asymmetric pay-off profiles) potentially embedded in a slightly broader portfolio context. By contrast, a basic degree of diversification significantly reduces the risk of both impairment from individual stocks, and from missing out on outlier gains that can accrue in unexpected ways in slightly broader portfolio.

As a firm, we're seeking to construct portfolios that provide a broad exposure to quality opportunities at the very small end of the equity capital market. It's an exposure that can be difficult and time-consuming to replicate, and often an exposure investors simply don't otherwise have. And it's an area where being active, including selectively participating in capital raisings, can genuinely add value to investment portfolios. By contrast, we believe it's very hard to differentiate and add value at scale and investing say in the top-20 listed companies. In that space, a low-cost passive approach may be more appropriate.

We believe casting the net relatively wide provides the best chance of capturing outsized returns from a number of outperforming individual companies, while at the same time, casting that wide net in a very carefully considered section of the capital market. Namely: across smaller companies that have underappreciated and undervalued growth

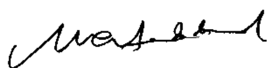
opportunities; sell for a low price relative to current sustainable rates of earnings; or are cheap relative to underlying (and genuine) asset value.

In Summary

With the portfolio invested across 37 different companies we're looking forward to the ongoing management process for the portfolio. We expect this will now feature some degree of selling (trimming or exiting) where a thesis has played out, or become impaired, or where we need funds for other opportunities. Our holdings include idiosyncratic positions within different buckets of opportunity, with no one sector or theme dominating the exposure set.

The base of the DMXASF portfolio is its strong overlap with the highly successful DMXCP portfolio. Many of the companies in the DMXCP portfolio can be scaled to some degree, and we're glad to have DMXASF able to take advantage of the opportunity to deploy more funds into many of the interesting companies that DMXCP owns. On the other hand, many of DMXCP's positions are illiquid and not appropriate for DMXASF. We look forward to continuing to build and run a portfolio at DMXASF that effectively captures what's readily available from DMXCP (from a liquidity perspective) and complementing these with an interesting selection of slightly larger and more liquid companies. All the while, staying true to the core investment philosophy we've refined over the past six years at DMX.

Kind regards



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