DMX
ASSET MANAGEMENT

DMX Australian Shares Fund

Investing in the most compelling Australian smaller company opportunities

DMX Australian Shares Fund

May 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 (30 April 2021)	**$1.0277**
Unit price (mid) based on NAV (31 May 2021)	**$1.0401**
Number of Stocks	36
% cash held - month end	19%

1-month return	1.21%
Since inception (1 March 2021)	4.01%
Fund size (gross assets)	$6m

Dear Investor,

DMXASF's NAV increased 1.21% (after fees and expenses) which compares to the ASX 200 Total Return Index's 2.33% gain. We continue to identify companies to add to the portfolio, and have slowly added to a number of existing positions. Just three months in with this new fund, we're pleased to be 81% invested across a broad range of interesting and diverse opportunities. Of that 81%, around 55% is in companies also owned by DMX Capital Partners (DMXCP).

Portfolio Commentary

The Fund's modestly profitable finish to the month (up 1.2%) doesn't reflect either the intra-period volatility (the Fund was tracking down 2-3% *within* the month) or the significant range of movements across portfolio constituents.

While the broad market continues to rise, we're witnessing increased dispersion across the market with certain segments and stocks declining meaningfully, while others continue to race ahead. Our portfolio was impacted in particular this month by the shift in sentiment away from technology focused companies, and those with long-tailed earnings streams. As was the case for DMXCP, exposures to **Knosys**, **Raiz Investments** and **CV Check** detracted as these fell 11-22% each). In addition, we own **Elmo Software** which declined 19%. On the other hand, within the space, our holding in **Gentrack** returned 32% on the back of a half year result ahead of guidance, and was a key contributor for the month.

Gains were recorded in a number of holdings, including:

- **LaserBond**, rising 22%. LaserBond is a leading specialist surface engineering company, focused on the development and application of specialised coatings that improve the efficiency and lifespan of capital-intensive machinery components. The company has been steadily growing on the back of its market-leading technology, but its focus in recent periods has been on licensing of this technology in order to accelerate that growth trajectory. LaserBond's business is supported by an impressive line-up of industry titans including Rio Tinto, Visy, Caterpillar and Bluescope Steel. But upside tail risk is inherent with the potential to license. This month, the company secured a multi-million dollar license agreement with a North American manufacturer of high-performance products. The win was powerful for the business for three reasons: (1) its sheer size and revenue/earnings contribution on its own; (2) the significant third party endorsement of LaserBond's innovation and technology; and (3) confirmation of the effectiveness of the company's sales and marketing strategy. The 22% share price rise over the month reflects this development, as well as the company's confirmation of strong growth in addition to this license agreement.

- **Shriro**, rising 21%. Shriro is a distribution company with rights to distribute Casio watches within Australasia, and having significant appliance and BBQ distribution businesses. Within its core appliance business, it sells directly to property developers for new homes, as well as – significantly – into retailers such as Harvey Norman. The company faces headwinds in areas, with, for example, its Casio distributorship being at risk should Casio decide to go it alone. But there are bright spots including with its BBQ distribution business into North America, and a favourable trading environment for its core appliance business in Australia. We purchased Shriro in March at 85cps on a single-digit multiple of normalised earnings. Where we believe the market sees a low quality 'distribution business', we see an important component within the supply chain of its key customers. For bulky household appliances, the company provides an outsourced fulfillment and logistics solution to major retailers – a service that is difficult to replicate or replace when operating at scale. Where the market saw a value-trap and share price that had done nothing in 5 years, we saw a highly cash generative business with a now-robust balance sheet, paying an 8% franked dividend, and building significant per-share tangible book value. Its recent share price strength has been on the back of positive commentary at its recent AGM, including articulating strategies for both organic and potential inorganic growth. And while now some 35% above our entry point, we believe still a very attractive price for this underappreciated asset.

With continued flows into the Fund from new and existing investors, how we're managing the various price movements for now is simply to focus on selectively topping-up laggards, while not needing to trim winners just yet as inflows are doing that work for us. Examples among detractors include **Raiz**, where we initiated a small position during the month around the time of its capital raise. We added to that position as its shares subsequently declined. Similarly, **Elmo** was initiated in April in the $5-range, and now in the $4-range we've added to this position. In both cases, the declines were as a result of poor market sentiment in the sector rather than any stock specific factors. We view this sort of volatility as a buying opportunity and are pleased to be able to continue adding to these as well as other sensibly-priced, high growth companies.

<u>New Position: Earlypay</u>

As we seek to add interesting, differentiated, and highly prospective companies to the portfolio, we're pleased to highlight a recent addition: Earlypay. Earlypay provides Invoice Factoring and Equipment Finance to small and medium-sized enterprises (SMEs). The Factoring industry is well established, and value-adding for many businesses who can effectively borrow against their trade receivables in order to improve cashflow. Equipment Finance is a similarly value-adding financing option for many businesses, allowing them to finance important capital investment. While lending to SMEs can be risky, we take comfort from the secured nature of Earlypay's lending focus, together with historically very low loss rates.

Last year, following a failed takeover attempt from a competitor, the company went through a significant transformation. A strategic acquisition of a smaller online lending platform was made, allowing the company to expand their customer reach and lending range (to smaller loans). The new technology platform seamlessly plugs into clients' accounting systems (such as xero, MYOB etc) enabling visibility over new invoices and efficient approval for funding. This technology platform enhancement led to a brand re-boot with the company changing its name from CML Group to Earlypay, and triggering the corporate equivalent of a cultural renaissance with the CEO ditching his suit & tie in favour of an Earlypay-labelled T.

A recent management meeting with CEO, Daniel Riley, and Chief Commercial Officer, James Beeson, reaffirmed the investment thesis and highlighted the very real potential for growth this prudently managed financier has in the years ahead. Having recovered from a COVID-induced slowdown last year, Earlypay's loan book is now at record highs. Growth is being fueled by reduced wage subsidies, as well as its new digital offering. 90% of new clients are now onboarded via its new online platform. This low-friction sign-up process and fast lending decisions for direct customers and brokers highlight Earlypay's credentials as an emerging 'fintech' and is giving them an edge over their traditional competitors. Importantly, the more stream-lined sign-up process has reduced the administrative burden on the company allowing for a greater investment in business development resource. Management have indicated this pivot in focus should help underwrite continued growth in the periods ahead.

Earlypay's market valuation remains very sensible at around 10 times our expectations for 2022 earnings, and with significant free cashflows. The market continues to value the business as a stodgy financier, and we believe is failing to acknowledge the technological overhaul and associated very real potential for growth.

<u>In Summary</u>

At 81% invested, we consider the implementation phase now effectively complete for the Fund, and are very much focused on the opportunistic management of positions across our broad range of interesting holdings. Overall, we are pleased with the balance of sectors, styles, and value within the fund, and continue to look for quality additions for the portfolio.

We continue to welcome new investors to the Fund, and thank both new and existing investors for your support and confidence through this establishment phase of the Fund.

We welcome the opportunity to speak with existing or potential investors at any time.

Kind regards

Michael Haddad	Chris Steptoe
Co-Portfolio Manager	Co-Portfolio Manager