DMX
ASSET MANAGEMENT

DMX Capital Partners Limited
Investing in the most compelling nano and micro-cap opportunities

DMX Capital Partners Limited
May 2021 – Investor Update

An investment company managed by:
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DMXCP directors: Roger Collison
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Opening NAV (1 May 2021) [1,2]	**$2.8092**
Closing NAV (31 May 2021) [1,2]	**$2.8401**
Fund size (gross assets)	$20m
Gearing	nil
% cash held - month end	11%

1-month return	1.10%
3-month return	5.59%
12-month return	81.22%
3-year return (CAGR p.a.)	24.61%
Since inception (*6 years & 2months*) (CAGR p.a.)	22.24%

*DMXCP Share price = Closing NAV (**$2.8401**), being: Share portfolio value + cash – fees payable – tax payable + franking credits*
Returns include dividends reinvested and franking credits paid. Since inception 41c of dividends & franking credits have been paid

Dear Shareholder,

DMXCP's NAV increased 1.10% (after all accrued performance and management fees and expenses) for May 2021. The NAV as at 31 May 2021 was **$2.8401**, compared to $2.8092 as at 30 April 2021. The All Ordinaries was up 1.59% during May, the ASX Small Ordinaries Index increased 0.18%, and the XEC Emerging Companies Index was up 1.96%.

DMXCP has returned 69.74% for the financial year to date (since 1 July 2020) (after all accrued performance and management fees and expenses).

May Portfolio Developments

The DMXCP portfolio finished May modestly up, following another month relatively light on portfolio news.

Holdings that contributed positively to the month's result included ICS Global (ASX:**ICS**; up 12% and discussed in more detail below) and Cryosite (ASX:**CTE**; up 30%).

Key detractors came from our basket of smaller, technology focused positions. Knosys (ASX:**KNO**; down 22%), 8Common (ASX:**8CO**; down 20%) and Raiz Invest (ASX:**RZI**; down 14%) all fell on no news when sentiment turned negative towards technology names during the month.

ICS Global – a surprising new substantial holder

We have previously noted our position in ICS, where we own just under 5% of the company. ICS is currently a cash box with ~$23m of cash (and a $23m market cap). Once a substantial cash return to shareholders is completed in July, we expect that it will look for new opportunities to 'back-door' into it.

ICS had one of the more intriguing announcements during the month when Damian Banks emerged as a substantial shareholder of ICS with a 7.5% holding. We know Damian from his time at Konekt (ASX:**KKT**), where he had initially bought himself a holding below 5c in 2011, then, joined as its Managing Director, and helped drive the growth of the business through to its eventual sale to private equity at 70c in 2019. We were shareholders in KKT from 2015 to 2019. We look forward to further interesting developments here.

Exposures that are different

We are passionate about identifying and owning interesting exposures that are not only attractively valued and compelling, but that are also different and often difficult for many investors to otherwise access. In doing so, we believe we can add real value to an investor's broader investment portfolio through genuine differentiation and diversification, as well as achieving potentially attractive long term returns. We prefer to be invested in these sorts of 'different' opportunities, rather than other higher profile stocks that are more widely held by other investors and fund managers.

Typically, we achieve this objective of owning 'different' exposures through investing in interesting, under-the-radar, and often illiquid, nano and micro-cap companies listed on the ASX. We also review numerous unlisted and pre-IPO opportunities, although we generally struggle to get comfortable with the business model and/or valuation of most of these opportunities. We do, however, have exposure to some companies that are not currently traded on the ASX. One such portfolio position is Tambla Limited, a company that was previously listed, but which is now an unlisted public company, and which we discuss below.

Background

We first discussed our position in Tambla in July 2019, when DMXAM became a substantial shareholder in the company. At the time we described Tambla as *"a software company that provides enterprise grade workforce solutions to organisations with large shift-based workforces, such as those in the aged care or transport sectors…Tambla has a global customer base of over 200, with tier one enterprise customers including K-Mart, Sydney Buses and Sydney Trains. Customer retention is at 95%... The business is currently EBITDA, operating cashflow and NPAT positive, and our discounted cash flow valuation is materially higher than where the stock is currently trading"*

Despite these positive attributes, a lack of organic revenue growth, regular calls on capital to fund a large R&D spend, and very poor liquidity saw the TBL share price continue to languish.

2020: delisting from ASX, capital raise and DBS acquisition

In June 2020, Tambla delisted from the ASX, supported by 95% of shareholders. The reasons given by the Tambla Directors for the delisting included:

- a share price which was not equivalent to comparable valuations in private companies meant (despite strong industrial logic) **numerous M&A opportunities stalled over value**;
- being listed (and having its financials easily observable) was detrimental to Tambla winning new enterprise business; and
- compliance costs associated with listing would be eliminated (estimated at ~$400k to $500k per annum).

Delisting the company was seen as the best way to recognise medium term shareholder value; in particular, by allowing for M&A opportunities to be conducted outside of the public markets so Tambla's value would no longer be pegged to what the Directors viewed as an undervalued ASX share price.

In conjunction with the delisting, Tambla undertook a capital raise through an issue of convertible notes, offering a 6% coupon. We participated in this raise, given the attractive enterprise valuation, and on the understanding that there could be a liquidity opportunity (through the potential sale of Tambla) in the future. We continue to hold these convertible notes, and should we choose to convert them, it will materially increase our equity exposure to the company.

With an improved cash position, Tambla was well placed to execute an opportunistic acquisition in September 2020 when NZ based IT company Datacom, was looking to divest a non-core Australian asset - *Datacom Business Services* (DBS), a Victorian SAP payroll managed services company focused on government and enterprise customers.

A highly strategic and complementary acquisition

The acquisition of DBS on 1 September 2020 has resulted in a significant step-change to the Tambla business:

- DBS provides a complementary tech stack and solutions that 'book-end' the core Tambla solutions (discussed below);
- DBS has a highly complementary enterprise and government customer base, and provides Tambla with a strong Victorian presence and business development team; and
- The acquisition doubled Tambla's revenue and is expected to generate ongoing cost synergies that should have a positive impact on Tambla's profit as they are realised over the next 12 months.

Tambla's core technology, developed over the last 20 years, has been its workforce management solutions for large (1,000 employees plus) businesses that have complex, shift-based workforces on different awards. The core Tambla HR solutions encompasses software that enables workforce planning/forecasting, scheduling and rostering, time and attendance recording and leave/entitlements management, with a particular emphasis on sectors that are subject to multiple awards and complex pay structures. The software ensures visibility, optimisation and compliance of workforces.

The DBS acquisition is very complementary as it now allows Tambla to also offer a specialist out-sourced enterprise payroll solution (payroll management and automated payroll processing – powered by SAP software). This offering sits behind (and integrates with) the traditional Tambla rostering and time & attendance software, enabling Tambla to process pay-runs – so Tambla no longer just supplies the data that feeds into the payroll calculations. The DBS acquisition also allows Tambla to offer a Human Resources module (onboarding, training/learning and development) that sits in front of the core Tambla offering.

There is cross-sell potential to further integrate the traditional Tambla software solutions with the existing SAP software of the DBS customers, as well as offering upgraded payroll services to the existing Tambla customer base.

The business and customer integration of Tambla and DBS is a significant ongoing project, but to date (since September 2020) DBS has delivered results that have been in line with its forecasts and this is expected to continue.

According to Tambla, it is now the only Australian owned provider of a complete workforce management software solution (that integrates human resources, staff planning/ rostering, time & attendance recording, and management and processing of payroll), specifically focused on large enterprise and government workforces. The majority of Tambla's forecast $20m+ revenue in FY21 will be generated from government and health sector enterprise customers.

Today

The DBS acquisition has provided Tambla with increased scale and credibility as an enterprise HR software company:

- Current revenue run-rate exceeds $20m, of which ~75% is recurring revenue;
- Customer retention is at 95%, with a strong Tier 1 customer base, including K-Mart, Starwood Hotels (Sheraton, Westin) and a number of federal, state and local government departments and enterprises;
- The company is currently generating 15% EBITDA margins, and is trading profitably at the NPAT level;
- Tambla is expected to be generating positive free cash once one-off acquisition integration and data-centre relocation CAPEX has been completed;
- Expectations are for continued annual double digit organic revenue growth.

These are attractive fundamentals for a company that had a **market capitalisation of $3m** when it delisted a year ago.

Where to from here?

We expect the end game here to be the eventual sale of Tambla. A recent option package incentivises senior management to achieve a sale within the next 3 years.

Potential acquirers of Tambla may include:

- another Australian enterprise/government focused software company attracted to Tambla's customer base and enterprise level software;

- a mid market focused HR tech company looking to enter the enterprise space; or
- an offshore HR software company looking for Australian exposure.

The HR/payroll technology sector continues to see significant consolidation and M&A activity. Some of this activity observed on the ASX over last 12 months is listed below.

Acquirer	Target	Transaction value	Revenue multiple	EBITDA multiple	Description
ASX:PYG[1]	Integrated Workforce Solutions	$15.3m[6]	2.8x FY21 ARR	14x FY21 EBITDA	Payroll and rostering for franchises in ANZ
ASX:CV1[2]	Bright Technologies	$15.3m	3.1x FY20 revenue	9X FY20 EBITDA	HR compliance and management platform
ASX:PYG[3]	PayrollHQ	$2.5m	1.7x revenue	*EBITDA not disclosed*	Small outsourced payroll provider
ASX:ELO[4]	Breathe	$39.6m[6]	6.1x ARR	Not EBITDA profitable	UK self-service HR Platform for small businesses
ASX:PYG[5]	TalentOz	$1.7m	1.7x SAAS revenue	*EBITDA not disclosed*	Malaysian cloud-based HCM and payroll software

1. ASX announcement released by ASX:PYG on 31 March 2021
2. ASX announcement released by ASX:CV1 on 10 February 2021
3. ASX announcement released by ASX:PYG on 4 November 2020
4. ASX announcement released by ASX:ELO on 7 October 2020
5. ASX announcement released by ASX:PYG on 14 July 2020
6. Includes earn-outs

The pricing for these transactions is typically being disclosed to the ASX on an EV/revenue basis. Further, our understanding is that global payroll companies are looking to pay around <u>3x FY22 EV/revenue</u> to acquire well run regional businesses. This multiple is broadly consistent with the multiples of those larger transactions observed on the ASX recently as noted above.

Tambla is currently valued in the DMXCP portfolio on a mid-single digit EBITDA multiple. This equates to an enterprise value of <u>less than 1x FY21 revenue</u> – significantly lower than the revenue multiples observed in the transactions noted above. We also note that Paygroup Limited (ASX:**PYG**), a similar sized business to Tambla, but in our view, a lower quality comparable, trades on 12x FY22 EBITDA – around double that of our current carrying value for Tambla.

Management still has much work to do, to continue to execute and achieve a sale. However, we are increasingly optimistic about a positive outcome and potential valuation uplift here.

As mentioned above, we aim to provide our investors with exposure to interesting, under-the-radar companies, that have attractive upside within a diversified portfolio that is difficult to replicate. We think our equity and convertible note investment in Tambla is a good example of an interesting and 'different' opportunity, as is ICS which we also mentioned above. We remain focused on actively managing a diversified portfolio of these interesting exposures with attractive risk reward characteristics.

We note that DMXCP's net assets are currently ~$19m. We continue to target a close for DMXCP <u>to new investors</u>, at $20m. Capacity for <u>new investors</u> is limited. If you are <u>a Sophisticated Investor</u>[5] that has interest in investing in DMXCP, we encourage you to contact us.

We look forward to updating you in early July with further portfolio news.

Kind regards

Roger Collison	Steven McCarthy	Chris Steptoe
Chairman	*Portfolio Manager*	*Research Analyst*

Note 1: Net asset value (NAV) is after all tax accruals but includes an estimate of franking credits available. Refer note 4, unaudited
Note 2: Unaudited result
Note 3: All DMXCP disclosed returns include the payment of dividends and franking credits
Note 4: Franking credits per share are franking credits arising from dividends received and for tax paid or payable on realised portfolio gain
Note 5: a gross income of $250,000 or more per year in each of the previous two years, or net assets of at least $2.5m (Corporations Act reg 6D.2.03 and reg 7.1.28)

Appendix 1: Performance

Monthly DMXCP Net asset value (share-price) returns (after fees) since inception (April 2015) [3] (%):

Month	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	All Ords
2015	n/a	n/a	n/a	+0.201	+9.448	+1.104	+6.524	+1.971	+9.711	+0.958	+3.568	+2.470	**+41.62**	**-8.83**
2016	-3.590	+1.323	+2.049	+2.045	+2.143	+0.020	+5.389	+7.056	+2.156	+1.058	+1.520	+0.321	**+23.10**	**+7.01**
2017	+0.885	-0.816	+1.790	-0.741	-1.990	+0.210	+1.071	+1.208	+0.822	+3.494	-0.267	-0.055	**+5.54**	**+7.83**
2018	+0.445	-1.625	+0.008	-1.173	+0.310	-0.211	+1.017	+4.112	+1.604	-3.438	-2.827	-2.257	**-3.66**	**-7.24**
2019	+0.122	-0.010	-1.624	+3.754	+3.014	+0.418	+7.482	-0.889	+3.279	+4.567	+2.997	+0.140	**+25.10**	**+19.02**
2020	+2.33	-8.42	-17.91	+8.521	+4.525	+6.213	+10.09	+8.669	+6.518	+11.10	+7.86	+2.24	**+42.47**	**+0.72**
2021	+1.02	+3.31	+1.17	+3.20	**+1.10**								**+9.01**	**+8.11**

The following chart illustrates the return from investing $100,000 in the fund (including dividends and attached franking credits) since inception (1 April 2015). DMXCP is an absolute return fund, focused on generating positive absolute returns over the medium to long term.