DMX ASSET MANAGEMENT

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

DMX Capital Partners Limited
November 2021 – Investor Update

An investment company managed by:
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DMXCP directors: Roger Collison
Dean Morel
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Opening NAV (1 November 2021) [1,2]	**$3.1252**
Closing NAV (30 November 2021) [1,2]	**$3.0989**
Fund size (gross assets)	$25m
% cash held - month end	5%
Gearing	Nil

1-month return	-0.84%
3-month return	8.65%
12-month return	30.88%
3-year return (CAGR p.a.)	31.69%
Since inception (*6 years & 8months*) (CAGR p.a.)	23.05%
Since inception (*6 years & 8months*)	298.71%

*DMXCP Share price = Closing NAV (**$3.0989**), being: Share portfolio value + cash – fees payable – tax payable + franking credits*
Returns include dividends reinvested and franking credits paid. Since inception 81c of dividends & franking credits have been paid

Dear Shareholder,

DMXCP's NAV decreased 0.84% (after all accrued performance and management fees and expenses) for November 2021. The NAV as at 30 November 2021 was **$3.0989** compared to $3.1252 (ex-dividend) as at 30 October 2021.

In relation to the broader market, the All Ordinaries was down 0.67% during November, while the ASX Small Industrials Index decreased 1.54%.

<u>November Portfolio Developments</u>

November saw a number of smaller holdings that had performed strongly in recent times give back some gains. Aeeris (ASX:**AER**), Knosys (ASX:**KNO**), 8Common (ASX:**8CO**) and Xref (ASX:**XF1**) were all down between 15% – 20% on no material news. Strong performances were recorded by Maggie Beer (ASX:**MBH**) which was up 28% in November following a positive AGM update, while Janison Education (ASX:**JAN**) was up 20%.

November was again a busy month with AGMs and pleasingly across the portfolio trading updates provided were all generally positive. Some of the updates where we continue to see particularly attractive value and growth potential are discussed below:

- Sequoia (ASX:**SEQ**), the diversified financial services firm, noted strong operational progress and advised that its FY22 forecast EBITDA is on track to increase by more than 15% on FY21. At last year's AGM, SEQ guided for a 25% lift in EBITDA, but after three profit upgrades, actually delivered a 138% increase. We would expect SEQ to comfortably exceed this year's AGM guidance, and to deliver <u>a minimum 30% EBITDA</u> uplift for the year. On our forecast numbers, SEQ trades on a single digit NPATA multiple, and is one of our largest positions.

- AFL Legal (ASX:**AFL**), Australia's largest family law firm, reported first quarter revenue of $4.8m which equates to an annual run rate of $19.2m, up +17% against its pro-forma numbers (which include its recent acquisitions), suggesting meaningful organic growth. Underlying NPATA for the quarter was $0.7m, annualising this result, AFL trades on 10x NPATA with $5m net cash.

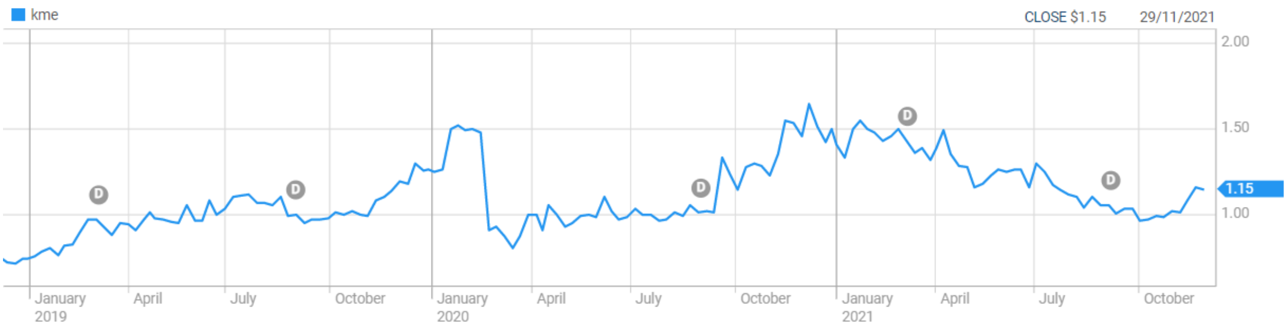
- Probiotec (ASX:**PBP**), the contract pharmaceutical manufacturer, advised that its first quarter trading performance was ahead of expectations and trading conditions are continuing to improve. Cough, cold and flu categories are showing early signs of recovery while PBP is expected to be a major beneficiary of the increasing onshoring of pharmaceutical manufacturing. PBP expects growth over its FY21 pro-forma NPATA of 18cps, suggesting it trades on ~11x NPATA.

As mentioned above, November was busy with many AGM and trading updates reported. With the Sydney/Melbourne lockdown restrictions eased, it was pleasing to be able to get back to face-to-face meetings, two of which we discuss below.

Kip McGrath Education Centres Limited (ASX:KME)

We attended the KME AGM in mid-November, which was an in-person event where the KME board, CEO and key management (CFO, CTO & COO) were all accessible to shareholders.

The KME share price has been weak over the past year, and, as illustrated below, has tracked sideways for the last three years. This lack of share price traction corresponds with three years of flat profit results, with COVID lockdown disruptions to face-to-face tutoring proving to be challenging for KME. KME has also undertaken a strategy shift towards a corporate delivery model (to complement KME's traditional franchise model) which is still in the early stages of being proven out.



We are confident that the company is well placed to resume earnings growth in the short term, and the KME story is starting to look particularly compelling for the medium term. Our confidence is supported by a number of positive earnings drivers and operational improvements that appear to be lining up nicely for the company:

- Post lockdown, there is strong demand globally for remedial learning, with parents concerned about the time children have spent out of school. KME lesson numbers have now returned to pre-COVID levels, with lesson numbers for Q1 of FY22 up 8%, notwithstanding the Australian and NZ lockdowns.

- The public education system is increasing its use of private tutors as governments devote more resources to lift children back to appropriate literacy and numeracy levels – KME's UK, US and Victorian businesses all have current tutoring contracts with schools, with KME expected to secure their first contracts with NSW Department of Education next year.

- KME's company owned tutoring centers are now operating at scale. In FY21 these corporate centres contributed a total of $3.7m revenue and generated a breakeven profit position. KME has guided for these revenues to increase more than 100% this year, with current run-rate suggesting corporate revenue in excess of $8m. At this level of revenue, corporate centres will contribute to group profit for the first time. KME group revenues for Q1 are up 21% driven by the growing corporate contribution.

- KME's new online US tutoring business (Tutorfly) is performing well and currently operating at breakeven, having benefitted from winning a material school tutoring contract. While we did have some initial concerns with this acquisition, revenues are ahead of expectations, and KME is planning for this operation in Houston to form the base of further expansion into the US.

- Over the last two years KME has invested in a stronger management team including a new CTO and COO. This has provided additional support to Storm McGrath, and has allowed more focused, management attention across all aspects of the KME business.

To attract investors back to the stock, KME needs to deliver earnings growth. Corporate-run centres should contribute to improved earnings this year. With further centre acquisitions planned, there is a clear pathway to double corporate revenues again to $15m over the next two years. At $15m revenue, the margins become material (30%+), and at this level, we expect that corporate centres would be delivering approximately half of group profits.

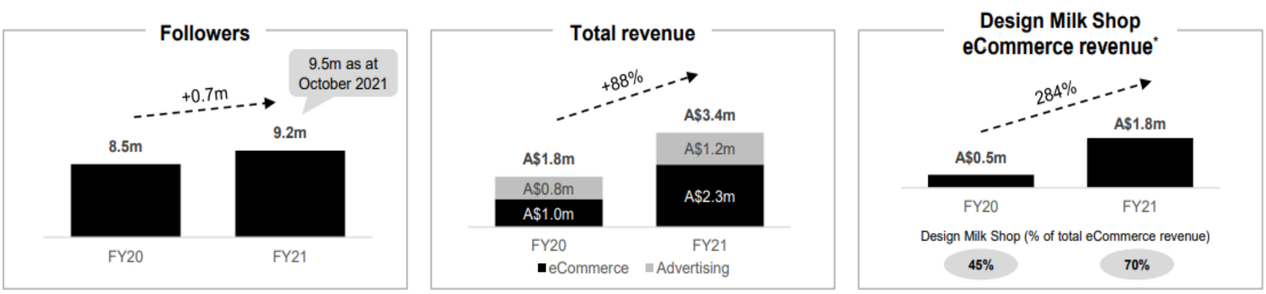
Another growth opportunity that KME has is to introduce Tutorfly (matching tutors with students for exam preparation primarily) into the Australian market, while taking the Kip McGrath brand (remedial tutoring) to the US to run a multi-brand go-to-market strategy in the medium term across various geographies.

In a post-lockdown world where there is increasing demand for remedial tutoring, we feel there are a number of growth opportunities for KME to take advantage of. We know families who have utilized the services of Kip McGrath and can vouch for the success of their methodologies. We are pleased to be long term supporters of a company that is making a meaningful difference to the outcomes of children, and look forward to the KME growth story playing out.

Design Milk Co Limited (ASX:DMC)

DMC is a relatively unknown, fast-growing, ASX listed company with its principal asset being design milk co - the largest design-led online brand globally (by number of followers). For anyone with an interest in architecture, design and new concepts, we highly recommend spending some time on this site (or download the design milk app). During the month we attended a broker hosted lunch where DMC was presenting.

DMC had a strong FY21, recording revenue growth of 88%, driven by the increasing monetisation of its audience through advertising and e-commerce. This impressive growth has continued into FY22 with Q1 revenues up 122% to $1.2m. The e-commerce opportunity here is Design Milk's boutique market-place where a curated portfolio of interesting design brands (currently ~500 suppliers) market their products to the DMC audience. The beauty of this model is that customer acquisition costs are minimal as DMC is able to sell to members of its large existing audience versus other e-commerce platforms that might be spending 10%- 25% of revenue on acquiring customers.



In 2019 when DMC bought the brand, it had 7.1m followers. This has increased to 9.7m followers today, while Management expect it to reach 10.3m followers early next year. The DMC audience continues to grow despite the move to monetise the website. The growth has primarily been driven by attracting new followers via social media through the provision of internally produced high quality editorial content, utilizing the strategy of 'content driven commerce'. DMC has a database of 225,000 of these historic articles and is adding 7 to 10 new editorials each week.

However, the DMC investment thesis is more than just about the eyeballs. We invested in DMC in the expectation that it was close to becoming cash flow positive. DMC should deliver its milestone first cash flow positive result this current quarter (which is a seasonally strong quarter due to Christmas). The challenge for DMC is then to continue that cash generation in the seasonally weaker months.

Notwithstanding a material increase in the revenues of the business over the past 18 months, Management has a number of levers to continue to drive further revenue and cash flow growth from here:

- There are currently 500 vendors available on the DMC market place – management plan to double that in the next 12 months. More products available for sale should lead to more sales, with DMC taking 40-50% commission on each sale.
- Business to business opportunities are also being progressed in order to provide more scale, with DMC well placed to 'connect' emerging design brands in their portfolio with US wholesalers/retailers, in addition to consumers. As a business focused primarily on selling into the North American market, DMC aims to have ~40% of their product sourced from Europe to offer unique and generally more 'edgy' products.
- Advertising opportunities, where gross margins are 90%, are being pursued with strong support from advertisers keen to get exposure to a large attractive demographic, as is sponsored media.
- DMC is also looking at affiliate publishing to assist in monetizing its substantial content library.

Despite its small size, DMC has strong supportive institutional holders on its register, including Bombora (17%) and interests associated with Thorney Investments (11%).

We believe there is significant strategic value in 1) the Design Milk brand (which is now in its 15th year); 2) its e-commerce platform; 3) the 10m (and growing) audience it commands and 4) its content library. With an EV of less than $15m and on the cusp of being cash flow positive, with very experienced and aligned management, we think DMC is an interesting, under-the-radar, opportunity.

As we close out an eventful 2021, we head into 2022 with confidence and look forward to continuing to provide our investors with exposure to interesting, undervalued, not widely known investment opportunities, underpinned by a disciplined and measured investment process. We thank all DMXCP shareholders for their support, and for the confidence you have shown in us and our strategy.

As this is the last newsletter before Christmas, we would like to take this opportunity to wish you and your family a safe and Merry Christmas and an enjoyable new year.

Kind regards

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

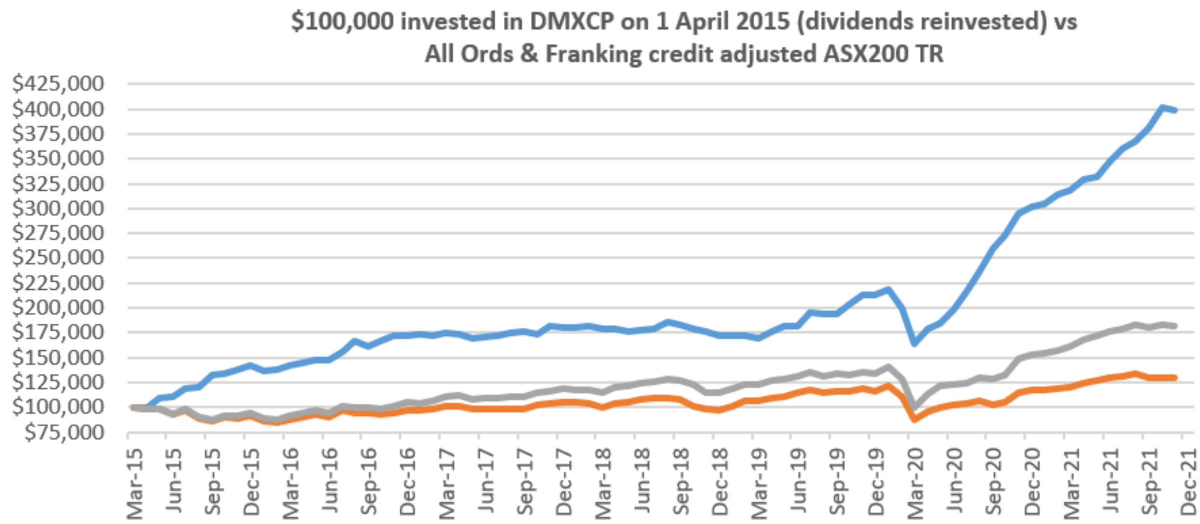
Note 1: Net asset value (NAV) is after income tax payable but includes an estimate of franking credits available. Refer note 4, unaudited
Note 2: Unaudited result
Note 3: All DMXCP disclosed returns include the payment of dividends and franking credits
Note 4: Franking credits per share are franking credits arising from dividends received and for tax paid or payable on realised portfolio gain

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	+0.70	+3.96	+2.12	+3.80	+5.51	-0.84		**+28.01**	**+10.74**

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.



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