DMX Capital Partners Limited
September 2023 – Investor Update

An investment company managed by:
DMX Asset Management Limited
ACN 169 381 908 AFSL 459 120
13/111 Elizabeth Street, Sydney, NSW 2000
DMXCP directors: Roger Collison
Dean Morel (Chair)
Steven McCarthy

Opening NAV (1 September 2023) [1,2]	**$2.3490**
Closing NAV (31 September 2023) [1,2]	**$2.4092**
Fund size (gross assets)	$23m
% Cash held - month end	2%
Gearing	Nil

1-month return	2.6%
3-month return	10.3%
12-month return	5.0%
3-year return (CAGR p.a.)	12.2%
Since inception (*8 years 6 months*) (CAGR p.a.)	15.5%
Since inception (*8 years 6 months*) (cumulative)	240.6%

*DMXCP Share price = Closing NAV (**$2.4092**), being: Share portfolio value + cash – fees payable – tax payable + franking credits*
Returns include dividends reinvested and franking credits paid.
Inception date of 1 April 2015 (Inception NAV: $1.00). Since inception, $1.02 of dividends & franking credits have been paid.

Dear Shareholder,

DMXCP's NAV increased 2.6% (after all accrued management fees and expenses) for September 2023. The NAV as at 31 September 2023 was **$2.4092** compared to $2.3490 as at 31 August 2023.

Markets continued to be weak in September - the All Ordinaries fell 3.6% while the Small Ordinaries declined 4.6%. The smallest companies on the ASX had another challenging month with the Emerging Companies Index falling 5.7%.

<u>September portfolio news</u>

After the conclusion of the August reporting season, September was a quieter month for company financial updates. However, we saw a number of positions subject to corporate activity, including takeover offers for two of our top 10 positions (Cirrus (ASX:**CNW**) up 43% for the month and Diverger (ASX:**DVR**) up 15%). Detractors for the month included Pure Profile (ASX:**PPL**) which was down 9%, Raiz (ASX:**RZI**) which fell 18% and PeopleIn (ASX:**PPE**) down 13% - each declining on no specific company news.

We mentioned last month, following the reporting of the FY23 results, that we were enthused with the value across the portfolio. In many cases, we think pricing and sentiment is at levels not seen since the days of Global Financial Crisis in 2007-2008. The current takeover interest and activity suggests that other industry participants and financial investors are also seeing this value. Unfortunately, this takeover activity is taking place when both share prices and earnings are subdued, and we consider that the takeover bids being received substantially undervalue the target companies relative to their longer-term value. Further, in the three instances below, as shareholders of attractive target companies, we are being offered scrip in larger companies that we consider to be less prospective. During the month we saw:

- CNW recommended a cash/scrip bid from larger listed IT services player, Atturra (ASX: **ATA**) on an FY23 EV/EBITDA multiple of 8.8x before synergies and an FY23 EV/EBITDA multiple of 7.0x including synergies. After pushback from CNW shareholders, the bid price was increased from 5.3c to 6.3c.

- Shareholders of DDH1 (ASX:**DDH**) voted in favour of being acquired by larger mining services operator Perenti (ASX:**PRN**) for a mixture of cash and shares. The acquisition multiple here was a low 5x EBIT multiple or 7x FY24 PER (pre synergies). The acquisition is expected to be double digit EPS accretive to PRN, with PRN looking to achieve ~$22m in post-tax synergies.

- DVR recommended a bid, again a mix of cash and scrip, from larger financial services business ASX-listed Count (ASX:**CUP**) on an FY23 EV/EBITA multiple of 6.6x (pre synergies). The transaction is expected to be 25%+ EPS accretive for CUP after realisation of cost synergies.

While it is encouraging to see interest in companies that we own, these bids are at levels well below our assessments of intrinsic value. Further, target company shareholders are not – in our view – being adequately compensated for a premium for control, nor the synergies and control of the cash flows that the acquirer will benefit from. DVR, which we discuss below, is the most disappointing bid of the three.

DVR's proposed acquisition by Count (ASX:CUP)

We have been shareholders in DVR since 2017. That year, DVR reported an underlying profit (EBITA) of $3.3m. DVR has reported strong growth since then. By FY20, EBITA had grown to $5.7m, and, at its most recent results, DVR gave EBITA guidance of $8m-$9m in FY24. We believe that with this demonstrated long term track record of significant profit uplift, DVR is a business with an attractive growth profile and strong and capable management execution. With 90% of its income recurring through ownership of some attractive assets such as its industry leading accounting training business, and its high margin investment management business CARE ($2.7b FUM), DVR has attractive qualitative aspects. However, while DVR's progress operationally has been strong, its share price has underperformed, with DVR's shares trading at similar levels today as they were back in 2017.

While DVR highlighted that the offer represented a 27% premium to its one-month VWAP, DVR's share price had been trading at such depressed levels in recent times, that this premium, in our view, does not result in a valuation that is close to what we believe to be DVR's intrinsic value. Given the disconnect between value and share price, we consider any reference to the historical DVR share price in the context of determining fair value is effectively redundant. As set out below, highlighting the farcical nature of the transaction pricing, based on publicly disclosed FY25 earnings targets, the combined CUP/DVR business is expected to be more expensive (5x EBITA) than DVR on a standalone basis (3.6x - 4.3x EBITA), even after the merged business benefits from $3m of synergies (which will cost $8m to deliver). While there are other benefits to the acquisition (improved liquidity, larger more diversified company) we struggle to see the value basis of this transaction from the perspective of DVR shareholders.

DVR's earnings profile, and implied acquisition multiples

	DVR FY23 actual	**DVR FY23 exit run rate**	**DVR FY24 guidance**	**DVR FY25 target**	**Merged CUP/DVR FY25 target**
EBITA	$6.9m	$8.2m	$8m - $9m	$10.5m - $12.5m	$22m+
Implied acquisition multiple (EV/EBITA)	***6.6x***	***5.5x***	***5.1x – 5.6x***	***3.6x – 4.3x***	***5x***
NPATA	$4.7m	$5.0m	$4.9m - $5.6m	$7.0m -$8.3m	
EPS (based on NPATA)	12.5cps	13.2cps	12.9-14.7cps	18 – 22 cps	
Implied acquisition multiple (PER)	***9.1x***	***8.6x***	***7.7x - 8.8x***	***5.2x – 6.3x***	

In its shareholder communication, the DVR board noted the acquisition multiple of 6.6x (based on FY23 EBITA of $6.9m). However, the FY23 earnings would appear to represent the low point in DVR's earnings cycle. Therefore, to us, it would seem inappropriate to base a transaction on these weaker earnings, given they do not include 1) the additional EBITA in acquired earnings during FY23; 2) the increased run-rate momentum of DVR in the second half of FY23; 3) the much-improved FY24 guidance provided to the market; and 4) the $3m in synergies available to CUP.

Indeed, if we were to adopt DVR's current earnings run rate (13.2c) then that level of earnings implies an acquisition PER (price earnings ratio) of 8.6x. If we look out to the FY25 target of ~20c EPS, then we have an acquisition PER of just over 5x. *Post synergies, these multiples significantly reduce even further to much lower, single digit PERs*. We struggle to reconcile these extraordinarily low acquisition multiples to DVR's growth profile and business quality and progress. We recognise that the EPS 'stretch' target for FY25 may be on the high side, but even achieving half the targeted uplift (i.e EPS of 16cps -17cps) over the next two years will result in DVR being incredibly good value at present levels ($1.05) and relative to a bid price of ~$1.15.

As such, we do not believe this transaction reflects the fair value of the DVR business, and that the 25%+ accretion to CUP's earnings that is expected to be generated as a result of the acquisition highlights the significant value that DVR is bringing to the transaction (and that DVR shareholders are not being appropriately compensated for), as a result of this low acquisition multiple and synergies.

We therefore cannot see sense in transacting at this price, when, based on current expectations, DVR's earnings are heading towards 20c EPS. As market sentiment towards small companies improves, and as DVR's strong growth trajectory returns, then this earnings growth should eventually drive a much stronger share price without DVR shareholders being exposed to any of the significant acquisition integration risks and costs.

We have provided this feedback to Diverger, and have advised the company that we do not intend to support the proposed scheme as it currently stands. Subsequent to the takeover announcement, DMXAM has increased its position in DVR to 5.2%, lodging a substantial shareholder notice on 3 October 2023. On the back of this, we've heard from a number of other shareholders who are similarly underwhelmed by the bid and are glad to hear we're looking for an improved offer.

As mentioned earlier in this letter, it is encouraging to see the corporate interest in a range of companies that we own, though it is particularly disappointing to see directors of our companies recommend that shareholders accept takeover bids, that in our view, significantly undervalue their company. Last month we discussed the potential takeover of Energy One (ASX:**EOL**) which is another example of a board that in our view, has taken a very short term view in relation to the value of their company and is choosing to sell the company at an in-opportune time.

As investors, in the event of a takeover, the easy option is to accept the bid and move on. Where we fundamentally disagree with the decision of a Board, as is the case with DVR and EOL, we are conscious of doing the right thing by our investors by voicing our feedback, engaging with the company and other shareholders to at least try to achieve a more reasonable and appropriate outcome.

We thank all our investors for your continued support and look forward to updating you again next month.

Kind regards

Roger Collison
Chairman - DMXAM

Steven McCarthy
Portfolio Manager

Chris Steptoe
Research Analyst

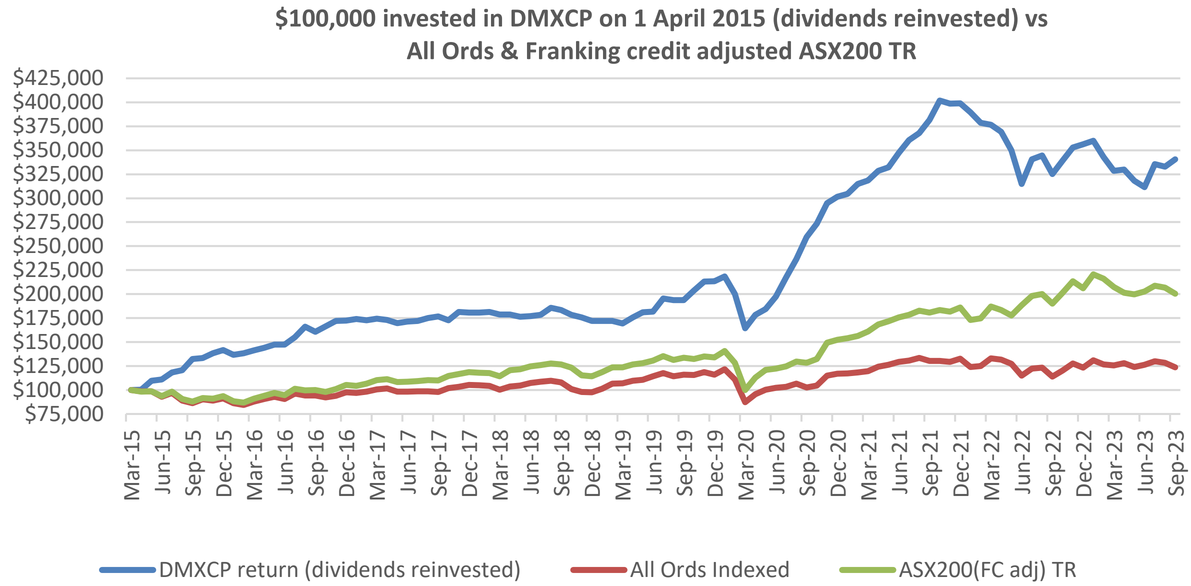
Note 1: Net asset value (NAV) is after income tax payable but includes an estimate of franking credits available. Refer note 4, unaudited
Note 2: Unaudited result
Note 3: All DMXCP disclosed returns include the payment of dividends and franking credits
Note 4: Franking credits per share are franking 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	+0.04	**+28.06**	**+13.55**
2022	-2.48	-2.93	-0.51	-2.04	-5.50	-10.64	+8.72	+1.20	-5.90	+4.52	+4.50	+0.96	**-11.4**	**-7.2**
2023	+1.12	-5.17	-4.52	+0.47	-3.94	**-2.30**	+8.55	-0.91	**+2.56**				**-4.7**	**+0.4**

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


$100,000 invested in DMXCP on 1 April 2015 (dividends reinvested) vs
All Ords & Franking credit adjusted ASX200 TR
$425,000
$400,000
$375,000
$350,000
$325,000
$300,000
$275,000
$250,000
$225,000
$200,000
$175,000
$150,000
$125,000
$100,000
$75,000
Mar-15
Jun-15
Sep-15
Dec-15
Mar-16
Jun-16
Sep-16
Dec-16
Mar-17
Jun-17
Sep-17
Dec-17
Mar-18
Jun-18
Sep-18
Dec-18
Mar-19
Jun-19
Sep-19
Dec-19
Mar-20
Jun-20
Sep-20
Dec-20
Mar-21
Jun-21
Sep-21
Dec-21
Mar-22
Jun-22
Sep-22
Dec-22
Mar-23
Jun-23
Sep-23
DMXCP return (dividends reinvested)
All Ords Indexed
ASX200(FC adj) TR