DMX Capital Partners Limited
January 2024 – 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 January 2024) [1,2]	**$2.2946**
Closing NAV (31 January 2024) [1,2]	**$2.3698**
Fund size (gross assets)	$23m
% Cash held - month end	6%
Gearing	Nil

1-month return	3.3%
3-month return	8.1%
12-month return	-3.1%
3-year return (CAGR p.a.)	3.4%
Since inception (*8 years 10 months*) (CAGR p.a.)	15.2%
Since inception (*8 years 10 months*) (cumulative)	249.4%

*DMXCP Share price = Closing NAV (**$2.3698**), 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 3.3% (after all accrued management fees and expenses) for January 2024. The NAV as at 31 January 2024 was **$2.3698**, compared to $2.2949 as at 31 December 2023.

After a strong December, Markets were mixed in January - the All Ordinaries was up 1.1% while the Small Ordinaries increased 0.8% and the Emerging Companies Index fell 5.2%.

Contributors to the portfolio for January included Findi (ASX:**FND**) which increased 57% following the conversion of options in the middle of January, which released the selling pressure on the stock experienced in the lead up to the conversion. Despite its strong recent performance, the stock trades below our $3 assessment of value, as discussed in our recent blog article. Medadvisor (ASX:**MDR**) also performed well, increasing 30% and reporting a first half result ahead of guidance. Detractors included Soco Corporation (ASX:**SOC**) which continued its fall from last month, declining 12% following a weak first half result, while Pharmx Technologies (previously Corum) (ASX:**PHX**) fell 17%.

Portfolio news – January

January saw many of our portfolio companies report their quarterly cash flow results for three months to 31 December 2023. In summary, we have generally seen improved results over recent months from these companies as revenues have grown and companies have taken costs from their often-bloated post-COVID cost base. While in many cases top-line growth has reduced from the levels seen between 2020 and 2022, particularly as economic conditions have tightened, we are happy to accept slightly lower growth rates providing companies are focussed on their cost base and running their businesses more efficiently and profitably.

Balancing profit and growth can be tricky, and Boards, Management teams and shareholders often have different perspectives on how to appropriately balance this dynamic. Businesses clearly need to look to the future and invest for the medium to long term in terms of new product development (capex, R&D) and business development (sales and marketing). But given the uncertainty around the payoff on much of this investment, our preference is for companies to take a more conservative and prudent approach in relation to this spending on future investment. We articulate this message to companies that we own, and that we'd rather see consistent 10%-20% revenue growth, with cost discipline and improving margins and profit, than a business that is investing (spending) heavily in sales and marketing that might generate one or two good years of 20%-30% revenue growth but often have no profit or cash generation at the end of the day to show for it, and eventually growth reverts to sub-par when they run out of cash to spend.

With those thoughts in mind, we look at how several of our portfolio companies are managing these challenges of investing for the long term versus generating near term profits, on the back of their quarterly reports.

Ansarada (ASX:AND)

Ansarada is a company we have owned and traded since its IPO in 2020, backed by a thesis that AND can replicate its market dominant position in deal data rooms in ANZ, in overseas geographies. It is a company that has always experienced tension between its investment spend and growing profits. When we initially spoke to Sam Riley, the AND CEO and founder, his view on the growth versus profits dynamic was encapsulated in his belief in the "rule of 40": that is, the sum of revenue growth % and EBITDA margin % should exceed 40. So, periods of strong revenue growth might be accompanied by a lower EBITDA margin and vice versa. However, with a collapse in deal activity in 2022 and 2023, the sum of AND's growth and margins was much closer to 20 than 40, and the market soured on the stock.

In its most recent quarter AND reported positive cash flow from operations of $5.7m, EBITDA margins at 21%, and growth of 10%, so the sum of growth and margins is heading back towards 40. However, the company did note increased marketing spend in the second half, which may impact EBITDA margins. In its outlook AND noted "*We have focused a lot on balancing operational efficiency and investment. This enables us to continue investing in early-stage products, pursuing the significant growth opportunities ahead of us, and maintain the optionality to deliver increased profitability over time*".

With $13.8m of operating cash generated by AND in CY23 (and free cash of $5.1m), at the low point in its business cycle, it would seem that AND is managing that balance between investment and profit in a relatively sensible manner. Given the high gross margins in the business of 95%, intuitively, there should be significant operating leverage within the business, and it makes sense to spend to capture that revenue, but at the same continue to drive margin improvement.

We look forward to seeing this operating leverage start to emerge in a more favourable environment for AND – key leading indicators including deferred revenue and new business wins are all trending higher, and well above current reported revenue growth rates, suggesting an acceleration of growth in future periods.

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Knosys (ASX:KNO)

KNO, which provides knowledge management, intranet and library management software solutions, pleasingly, confirmed the business was now profitable and that it was "*On track to deliver positive EBITDA in 1H FY24 and FY24*". All of KNO's development costs are expensed, so EBITDA essentially represents EBIT. We would expect KNO's full year cash EBIT to be between $500k to $1m, with Q1 EBITDA reported as $200k+. Free cash generated for the first half was ~$600k, with KNO having $3.9m of cash at the end of January (relative to its market cap of $6.2m).

This profit has been generated as a result of KNO taking a real axe to its cost base - operating cash outflows for the half of $4.7m were down 22%, with staff payments decreasing by 28% and marketing payments decreasing by 56%.

But while the business is now profitable, growth has stalled. Although KNO did note two new enterprise wins for the quarter, which should contribute to ARR growth once implemented; and that its level of tender activity remains strong, and the pipeline of qualified leads continues to increase across the business.

With its existing sales team and product investment spend, KNO is targeting 10% organic growth - which is on the modest side. However, as a high margin SaaS company (~90% gross margins), with lowish churn, if KNO can generate an additional $1m in annual revenue (i.e. 10% revenue growth), given the high gross margins, much of that incremental revenue should flow to EBIT, providing costs continue to be controlled. Therefore, even with modest organic revenue growth and given its current cost base, it is not difficult to see EBIT soon growing to $1m+. With the market currently valuing the KNO business at just over $2m, that would put it on a 2x EBIT multiple (KNO has significant tax losses and will not pay tax for several years). As it stands today, it is currently trading on 0.25x its $9.4m ARR.

In our discussions with management, we have, and will continue to, reinforce our view that KNO needs to continue to maintain a high level of cost discipline, ensure that they are getting the most they can out of their existing sales resources, and be focussed on generating increasing profits for the company. Consistent and growing profits is what we would expect to drive a strong market re-rate, particularly from a $2m EV. It is not unreasonable to expect a growing software business with $1m+ EBIT and $10m+ of ARR to have an EV of $15m - $25m rather than KNO's current $2m.

Careteq (ASX:CTQ)

During January we published a blog article on CTQ.

CTQ released its quarterly report, which was in line with expectations, with its operational targets re-affirmed. CTQ's core business, Embedded Health Solutions, (55% owned) continues to deliver free cash flow, and remains on track to achieve its $1.5 million EBITDA FY24 target. CTQ's Sofihub monitoring business continues to grow strongly.

While CTQ is still cash flow negative across the group, we are expecting an improvement from here. Management is confident that the foundations are now in place for profitable growth, with the targeted 15,000+ Sofihub subscribers combined with the anticipated EBITDA growth for Embedded Health Solutions expected to assist the company in achieving profitability leading into FY25.

DMXAM is the largest shareholder in CTQ, and we have made it clear to the company that the focus should be on reducing its cash burn as quick as possible and reaching the breakeven milestone by the end of the financial year as guided. And, if breakeven doesn't occur by then, we suggest CTQ look to sell its unprofitable Sofihub business, where we are aware that there is a natural buyer. Removing the Sofihub drag, and re-focussing on growing the profits from its EHS and HMMR referrals businesses and becoming self-funding, we believe would be well received. And even better if CTQ can increase its share of the EHS business.

Just as important as becoming profitable is then continuing to grow profits. Too many companies that we speak to think that when they reach a breakeven position, they can then put their foot back on the spending pedal as long as they maintain that breakeven result - a mindset that in our view generally encourages cost ill-discipline and poor investment outcomes. We have and will continue to make the point to CTQ Management (and various other management teams that we speak to) that the best way to grow a stock's value is by establishing a track record of consistently growing profits. Management has indicated that they want to get CTQ into the position that it can be paying dividends, which to us is an encouraging mindset in terms of how they are thinking about the future of the business.

With an EV of $3m, and with little success or expectation currently built into the CTQ valuation, we would expect a significant market re-rate when CTQ demonstrates its ability to become self-funding and is no longer perceived to be cum-raise.

2024

It has been a busy and productive start to the year for us:

- We are pleased to have been involved in the recent re-capitalisation of two (leading one of them) interesting sub-$20m companies on what we considered to be very attractive terms, that have very high IRR potential. We look forward to discussing these unique, prospective opportunities in future updates.
- In early January, we were required to decide whether to convert our significant FND option holding at 90c. To get more confidence around this position, as part of our continuing due diligence, we have had various meetings with FND's directors, its external accountant and other large FND shareholders. With the options convertible at 90c, and the share price having traded up to $1.70 post the conversion, we remain comfortable with our decision and our exposure here, having trimmed into the share price strength.
- We are also currently involved in progressive discussions with the directors, and other large shareholders, of several portfolio companies that we have held for some time, in relation to board composition and strategy, as we look to take a more active role in 2024 to extract shareholder value and improve investor outcomes across the portfolio, where we see the opportunity.
- We continue to review and meet with a number of prospective, unique investment opportunities.

In summary, the recent quarterly reports highlight many companies have taken tangible steps in relation to managing their cost line. Many of our nano-cap companies continue to trade at 24-month lows, on very beaten-up market valuations with many EVs still below $5m. From these low valuations, there is potential for significant share price appreciation, providing their management continue to deliver and execute from here. As noted, we are in close dialogue with many of these management teams, reinforcing the need for them to be focussed on establishing a track record of growing profits and prudent spending.

We thank all our investors for their support, patience, and for the confidence you have shown in us and our strategy.

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	-4.86	+4.06	+0.74	**-5.07**	**+8.4**
2 024	**+3.27**												**+3.27**	**+1.1**

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.