Emerging Companies Fund

Monthly Update: August 2021

Dear Fellow Investors,

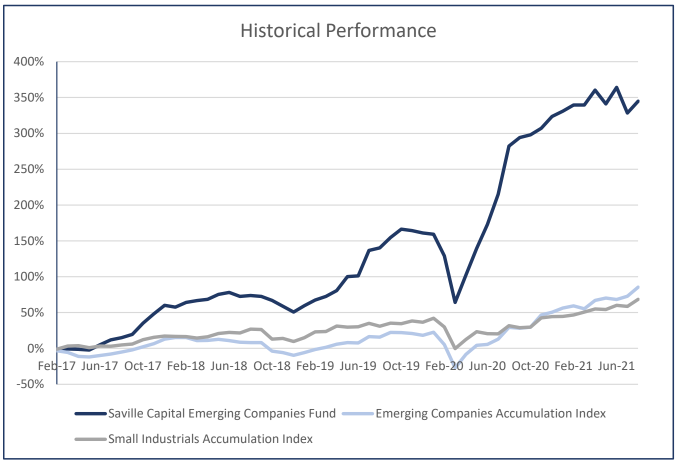
Our Emerging Companies Fund was up +4.3% in August vs +7.3% for the Emerging Companies Accumulation Index (XECAI) and +6.1% for the Small Industrials Accumulation Index (XSIAI). Since inception, the Fund has generated +38.5% p.a. and a total return of +344.8% vs +85.4% for the XECAI and +68.4% for the XSIAI.

Despite the solid positive overall result, it was principally due to just one stock, IDT Australia (IDT, +70%), which experienced a significant share price rally after announcing the finalisation of a Sterile Readiness Agreement with the Federal Government, to potentially produce a COVID-19 vaccine. As a reminder, we first bought IDT in August 2018 at ~$0.13/share (vs $0.695 at the end of August 2021), which is a significant return for the Fund. This is another example of the value of patience, underpinned by detailed research and high conviction on the long-term earnings and valuation potential. Unlike many other high growth stocks which have performed well for the Fund, IDT is/was a turnaround story which we bought at just above its NTA, with the view that under new management and with an improving operating environment, it would eventually find an opportunity to significantly increase the utilisation of its facility and return to sustained profitability. Unfortunately, many other stocks in the Fund continue to face a sentiment headwind, with almost half declining during the month. This seems counterintuitive based on the performance of the indices above, but the XECAI performance is largely coming from commodity stocks (e.g. lithium), while the XSIAI is comprised of much larger industrial stocks than those that we typically hold. For now, it appears that the industrial microcap universe is struggling to attract investor enthusiasm, which is often the case when the larger indices (and small cap commodity stocks) are performing well. The positive news is that these trends are cyclical, and we are still managing to perform “ok” through this period, primarily due to some very strong outcomes for just a few stocks.

Performance summary

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Total	3M	12M
2017		-3.2%	+2.6%	-0.6%	-1.0%	+7.6%	+6.4%	+2.7%	+4.0%	+13.2%	+9.5%	+8.1%	+60.1%		
2018	-1.6%	+4.2%	+1.6%	+1.1%	+4.1%	+1.6%	-3.1%	+0.7%	-0.8%	-3.2%	-4.8%	-5.2%	-5.9%		
2019	+6.0%	+4.8%	+3.1%	+4.7%	+10.8%	+0.6%	+17.6%	+1.4%	+6.1%	+4.6%	-0.8%	-1.3%	+73.2%		
2020	-0.6%	-11.7%	-28.4%	+23.3%	+18.4%	+14.1%	+16.0%	+20.7%	+3.1%	+1.0%	+2.3%	+4.0%	+62.3%		
2021	+1.9%	+2.1%	-0.1%	+5.0%	-4.4%	+5.5%	-8.0%	+4.3%					+5.6%	+1.2%	+16.9%

Returns are net of all base fees, performance fees and expenses of the Fund



Performance commentary

The three largest positive contributors comprised IDT Australia (IDT, +70%), Laybuy (LBY, +28%) and Pro-Pac Packaging (PPG, +22%). The three largest negative contributors were Imricor (IMR, -32%), Murray Cod (MCA, -6%), and Marley Spoon (MMM, -2%).

As already mentioned, IDT finalised a Sterile Readiness Agreement with the Federal Department of Health (“Health”) to bring IDT’s sterile manufacturing facility into a state of readiness to potentially produce a COVID-19 vaccine. The Sterile Readiness Agreement provides for an exclusivity period with the Australian Government for the use of IDT’s sterile manufacturing facility until the earlier of: executing a Supply Agreement for IDT to provide COVID-19 vaccine services to Health; or 4 months from completion of IDT's sterile readiness works (which will take another 1 to 2 months from now to complete). IDT’s sterile readiness activities are being undertaken on a “vaccine agnostic” basis, meaning that IDT will be readying the facility to potentially manufacture a COVID-19 vaccine which may be nominated by the Government at its discretion during the exclusivity period.

Further to this, IDT continues to progress with the Victorian Government and Monash Institute of Pharmaceutical Sciences (MIPS) on potentially providing cGMP manufacturing services for the production of MIPS’s receptor binding domain mRNA COVID-19 vaccine candidate. As evidence of its ongoing progress, a NanoAssemblr machine — a $1m nanoparticles processor used to produce mRNA vaccines — was recently sent to IDT’s facility, where it will be used to commence Phase 1 clinical trials of Australia’s first locally-developed mRNA coronavirus vaccine. The trial run of 150 doses of the locally developed vaccine candidate will be overseen by MIPS with $5 million of funding from the Victorian Government. According to the Government, the MIPS vaccine candidate is the leading one nationally, with clinical trials of the vaccine set to commence in October and the preliminary results expected by mid-2022. Finally, IDT returned to profitability in FY21, and with ~$7m cash in the bank, is well positioned to capitalise on these various opportunities.

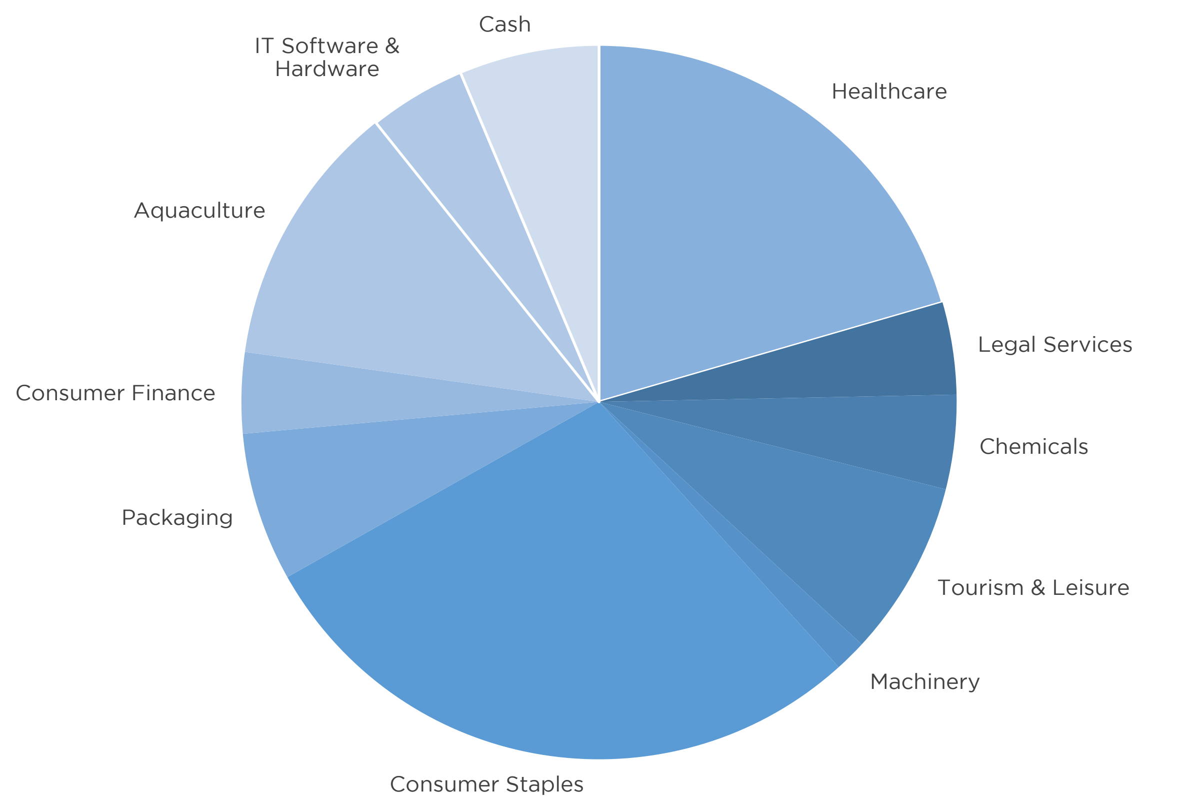
PPG reported an FY21 result which was comfortably ahead of our and broker expectations. The Company has come through a period of transformation in which it has forgone revenue growth to improve its margins and return on assets. With that process now largely behind it, PPG is expecting a return to revenue growth in FY22 while also delivering the full cost benefits ($7m p.a.) from its Chester Hill site consolidation. This should underpin ~20% growth in EBITDA and ~50% growth in NPAT during FY22, putting the stock on attractive FY22 multiples of ~4x EV/EBITDA and ~9x P/E, as well as an FY22 dividend yield of >4%. We also take confidence from the fact that directors (including the CEO) were buying stock after the result, as well its largest shareholder (entities controlled by Raphael Geminder), who now owns 52.7% of the Company.

Shine Justice (SHJ, +11%) also reported a very strong FY21 result, with its revenue and EBITDA for FY21 exceeding our own forecasts for not only FY21, but also FY22. SHJ continues to benefit from strong growth in its New Practice Areas, particularly Class Actions. Revenue growth of +6%, underlying EBITDA growth of +12% and dividend growth of +24% in FY21 serve to highlight the improvements SHJ is making to its business via higher margin work and better cash flow conversion. Despite its solid execution and guidance for low double digit EBITDA growth in FY22, SHJ continues to trade on very undemanding multiples. Based on our (and broker) forecasts it is currently trading on ~3.3x FY22 EV/EBITDA and with an FY22 dividend yield of ~5%. Assuming SHJ receives the remainder of its Mesh Case proceeds (~$20m), SHJ will have over $75m in cash to pursue accretive acquisitions and accelerate its already solid growth trajectory.

Finally, Tourism Holdings (THL.NZ, +3%) reported positive EBITDA (NZ$40.4m) and a modest operating loss (-NZ$14.5m) in FY21 despite incredibly challenging tourism conditions across its three key markets of New Zealand, Australia and the United States. With net debt at <NZ$50m (and undrawn facilities of ~NZ$200m), weakened competition and an optimised cost base, THL is very well positioned to capitalise on the expected gradual re-opening of these markets over the next 12 to 18 months.

Portfolio characteristics

We currently have ~94% of our capital invested in 15 stocks.



Please get in touch should you have any queries regarding the above. Thanks again for your interest and support and I look forward to providing another update in early October on our performance during September.

Kind regards,

Jonathan Collett

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