Emerging Companies Fund

Monthly Update: January 2022

Dear Fellow Investors,

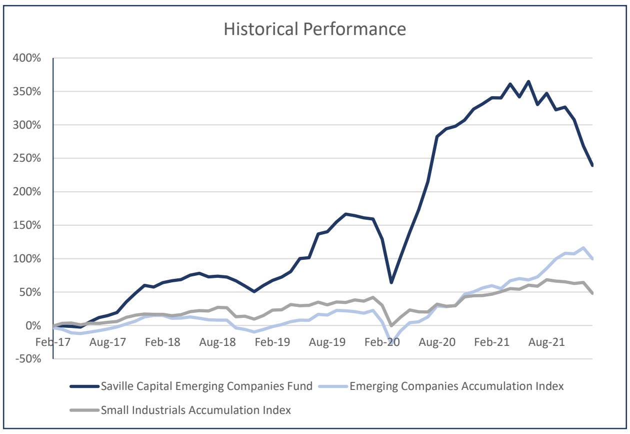
Our Emerging Companies Fund was down –7.9% in January vs -7.7% for the Emerging Companies Accumulation Index (XECAI) and -9.8% for the Small Industrials Accumulation Index (XSIAI). Since inception, the Fund has generated +27.7% p.a. and a total return of +239.4% vs +99.6% for the XECAI and +48.1% for the XSIAI.

Global markets nosedived in January on rising interest rate expectations and unfortunately our Fund was not spared any of the damage, albeit we are pleased to report that this trend hasn't continued into February (at least, not as yet). While we are always loathe to comment too much on market trends and outlook, given the significant moves we have now observed over the past six months in stocks that sit outside the mid to large cap space, we feel it is important to reiterate that business models that aren't yet profitable, are not broken simply because the 10 year bond yield moves from 1% to 2% or indeed even 5% (which is the risk free rate we adopt in our DCF models). Nor do we subscribe to the view that all long duration stocks were overvalued six months ago when bonds were 1% (which, ironically, remain very low at just 2%). There were, and still are, pockets of overvaluation among some stocks and sectors, but the purge of most stocks that are in the early stages of their growth profile simply because bond yields have (predictably) doubled off an unsustainably low base seems very short-sighted and without nuance. Ironically, the supply-side inflation pressures underpinning the moves in interest rate expectations are generally negative for mature business models where competition is more prevalent, margins are often lower and labour/capital intensity is higher. But up until now the narrative in response to this cycle of rising bond yields has been to sell stocks with growth/duration and buy value/cyclicals, which has heavily impacted our Fund given our micro/small cap strategy is naturally biased towards investing in the former.

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%	-5.5%	+1.0%	-4.5%	-9.6%	-13.0%		
2022	-7.9%												-7.9%	-20.5%	-21.3%

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



Performance commentary

The only positive contributor was Mighty Craft (MCL, +18%). The three key negative contributors were Marley Spoon (MMM, -31%), Universal Biosensors (UBI, -14%) and Lark Distilling (LRK, -13%), albeit most stocks in the portfolio were down between -5% and -15%.

MMM reported a much stronger quarterly result released after market on 31 January, so it isn't captured in this month's returns. MMM delivered record 4Q net revenue of €85m, up +24% on pcp with a contribution margin (CM) of 31% (just below its peak of 32% in 4Q CY20) and an EBITDA loss of -€4.8m. These figures compare very favourably with its 3Q result, which delivered net revenue of €79.2m, a CM of 28% and EBITDA loss of -€13m. The earnings and margin improvement came through a combination of price rises and cost discipline, particularly on marketing spend, the latter of which is foreshadowed to be kept in-check throughout CY22 and beyond. This result bodes well for MMM to meet its CY22 guidance of mid to high teens revenue growth, a CM of 29% and a maximum EBITDA loss of -€15m, which would lay the foundations for MMM to be EBITDA and cash flow positive in CY23. Note that this guidance excludes the expected positive earnings contribution from the Chefgood acquisition. While the stock has rallied in early February, it is still trading on just 0.4x CY22 EV/Sales and 1.4x CY22 EV/Gross Profit. These metrics are entirely incongruent with a company that continues to grow its revenue base (off strong comps) at healthy double digits, has addressed its margin decline through price rises and is now generating sequential improvement in EBITDA, with breakeven again within reach.

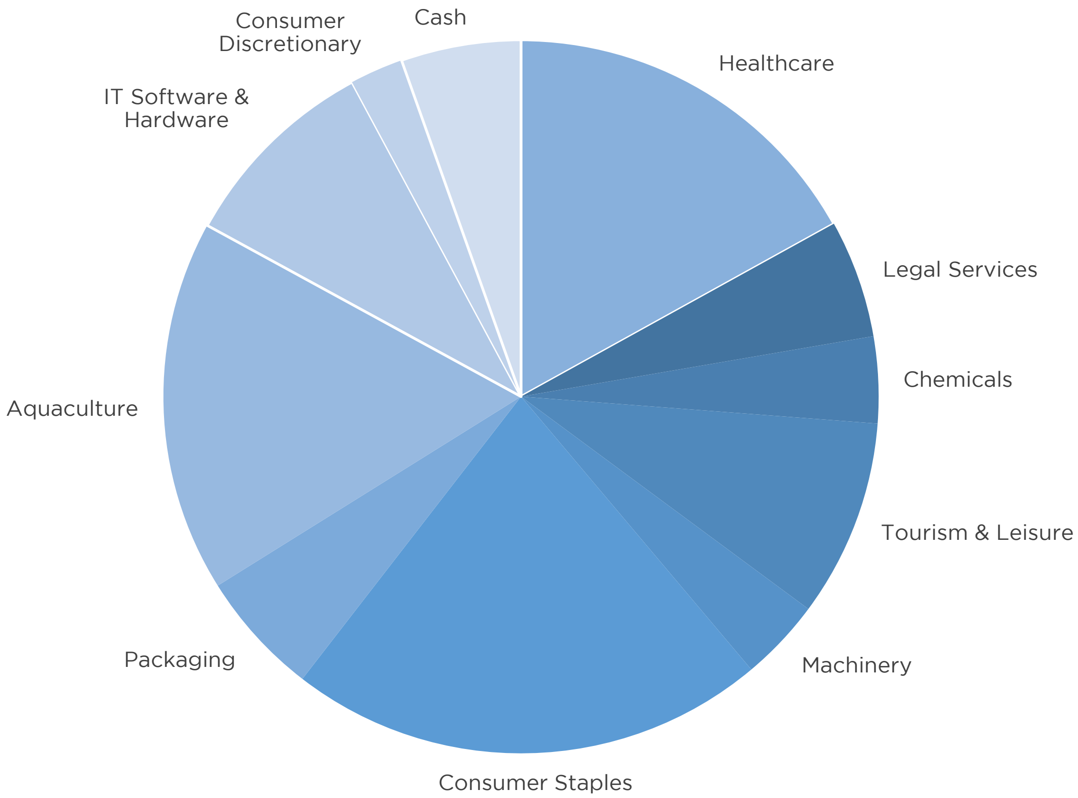
Ansarada (AND, flat) delivered an outstanding 2Q FY22 result (revenue +58% on pcp, +30% on 1Q FY22 and cash flow from operations +153% on pcp, +79% on 1Q FY22) with the share price now rallying strongly in February as the market fully digests it. We acquired our initial stake in AND during October 2021 (average entry was ~$1.80, share price is currently ~$2.40) and will discuss our investment thesis in more detail during our March Update (in early April). However, suffice to say, AND has many of the attributes we seek under our investment strategy, in that it is operating in a high margin/high growth industry (software-as-a-service), has market-leading technology in a large/global addressable market with inferior incumbents, has recently become EBITDA/cash flow positive, has no debt and is not well-owned by institutions nor well covered by brokers.

Hydration Pharmaceuticals (HPC, -10%) reported net revenue growth +44% on pcp in 4Q FY21 and gross margins increased to 43% (up from 24% in pcp), translating to gross profit growth of +78% on pcp. HPC continues to record EBITDA losses as it scales in North America, but we are confident its fixed cost leverage will enable it to start to generate positive EBITDA within the next year or two. Sales growth rates will be choppy while it cycles a period impacted by COVID-19, hence why we expect growth to significantly accelerate as we move into the next few quarters. HPC also signed a major distribution agreement with Chinese distributor, WPIC, which specializes in taking Canadian-based brands including Lululemon onto the B2C platform, T-mall. The partnership is a low-resource, fully outsourced China go-to-market strategy lead by a local Chinese team using predominately US inventory. New product innovation is continuing, with up to five new products expected to launch in the first half of CY22 across the US and Canada.

MCL also delivered a record outcome, with 2Q FY22 generating its first positive EBITDA result despite the ongoing impact of COVID-19 to its venues and on-premise sales. It also reduced its operating cash outflow to just -$1.6m, demonstrating the near-term potential for positive operating cash flow to be achieved. The highlight of the quarter was its Better Beer (zero carb beer) sales of $1.8m following its launch in November 2021. The success of the launch resulted in significant stock shortages, implying that sales to date are likely materially understated. The Company had previously provided an initial estimate of 3m litres of Better Beer sales in FY22, but this has already been upgraded to now be over 4m litres. MCL believes that Better Beer has the potential to be a significant national beer brand, as illustrated by the results in a recent Hottest 100 Craft Beers poll where it ranked #6 despite only just launching. If its growth trajectory continues, we think the value of MCL's stake in Better Beer has the potential to exceed MCL's entire current market cap.

Portfolio characteristics

We currently have ~94% of our capital invested in 16 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 March on our performance during February.

Kind regards,

Jonathan Collett

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Important Information