Emerging Companies Fund

Monthly Update: January 2024

Dear Fellow Investors,

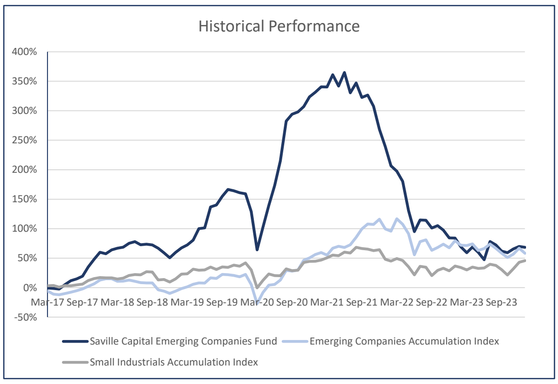
Our Emerging Companies Fund was down -0.9% in January vs -5.2% for the Emerging Companies Accumulation Index (XECAI) and +1.9% for the Small Industrials Accumulation Index (XSIAI). Since inception, the Fund has generated +7.8% p.a. and a total return of +68.4% vs +58.3% for the XECAI and +45.6% for the XSIAI.

We had hoped that the start of 2024 would bring a fresh, and more rational, perspective to Australian micro caps, however the trends of the past couple of years merely persisted during January. The broader market, including small caps, had another solid positive month, which continues to bode well for the inevitable catch-up trade in micro caps. But putting aside the index moves, this should have been a very strong month for the Fund given a major positive catalyst for one of our stocks, FBR Limited, finally materialised. Yet, because the announcement was coupled with a (modest) capital raise, not only was the stock unable to hold its initial gains (it peaked at +37% in early trading), it retreated back to the deal issue price before collapsing further to end the month down almost 20%, our largest negative contributor for January (incredible). If ever there was a perfect example of the ongoing challenges we are dealing with in micro caps, then I think this was it. Yet again, a desire for short-term (even immediate) liquidity trumped any rational view of (revised) current or future value. According to the implied logic of the market, the Company is actually worse off for having signed a transformative deal with the largest construction materials company in North America. Paradoxically, the stock is now trading at close to its all-time lows despite being in the best position it has ever been in with regards to commercialising (at significant scale) its robotic bricklaying machine. We will cover it in more detail over the page, but the silver lining is that the value created from this deal is not lost, it is just not yet recognised. Sadly, we require yet further patience.

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%	-9.6%	-3.0%	-5.8%	-17.6%	-15.5%	+10.1%	-0.3%	-6.1%	+2.0%	-3.8%	-6.7%	-49.9%		
2023	-0.2%	-8.1%	-6.1%	+6.1%	-5.4%	-7.8%	+21.2%	-3.7%	-5.6%	-1.8%	+3.9%	+2.6%	-8.1%		
2024	-0.9%												-0.9%	+5.7%	-8.8%

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



Performance commentary

The key positive contributors during January were Imricor (IMR, +8%), Ansarada (AND, +4%) and Murray Cod Australia (MCA, +3%). The key negative contributors were FBR Limited (FBR, -19%), Bluechiip (BCT, -19%) and Pentanet (5GG, -10%).

FBR announced the execution of a binding suite of agreements for a US Demonstration Program (to construct the external walls of 5-10 single storey houses in Florida) with CRH Ventures Americas, Inc. and the exclusive Option to then trigger a US joint venture. CRH is listed on the NYSE with a market capitalisation of ~US$50B and is one of the largest construction materials companies in the world, including operations in the US, Europe and Australia. Once the Option is exercised, a US$40m rolling loan facility will be established to fund construction of the Hadrian X® units and the JV will execute a binding conditional purchase order for 20 units. Two further conditional purchase orders of 39 and 40 Hadrian X® units will be placed subject to meeting utilisation and gross margin metrics (neither of which are onerous) on preceding orders, followed by options for a further 200 units. CRH subsidiaries will become the exclusive concrete block suppliers to the US JV and the parties will share in the profits generated from the JV as the units are hired out to US builders. To put all of this into context, the revenue potential of 300 units being deployed at 70% utilisation is in excess of US$1.1B pa, with target gross margins in excess of 50%. Unfortunately, FBR needed to raise capital (~$12m) to continue to fund its operations while the Demonstration Program is completed which, like so many other capital raises in the micro cap space over the past two years, resulted in a significant share price decline.

MCA resumed sequential quarterly growth during 2Q FY24, with customer receipts up +32% on 1Q FY24. This was driven by a combination of increased supply to the market (as has been foreshadowed by the Company) and ongoing price increases, with a +12.5% increase for large fish (>2.5kg) implemented during the quarter. Pleasingly, the 2023 spawning season was its highest spawning season to date, which creates the foundation for future volumes and growth which will be well in excess of current levels. The newly formed Australian Sustainable Protein Fund (ASPF) exchanged contracts to purchase the Stanbridge site (backed by a lease with MCA), which has development approval for 78 grow-out ponds and associated infrastructure, of which ~22 have already been constructed. These ponds are anticipated to be stocked with juvenile fish between February and April. Further to this, work is continuing on enabling the ASPF to accept investment capital from external investors so that MCA can then vend its own property and water rights into the vehicle, creating a cheaper source of capital for the Company.

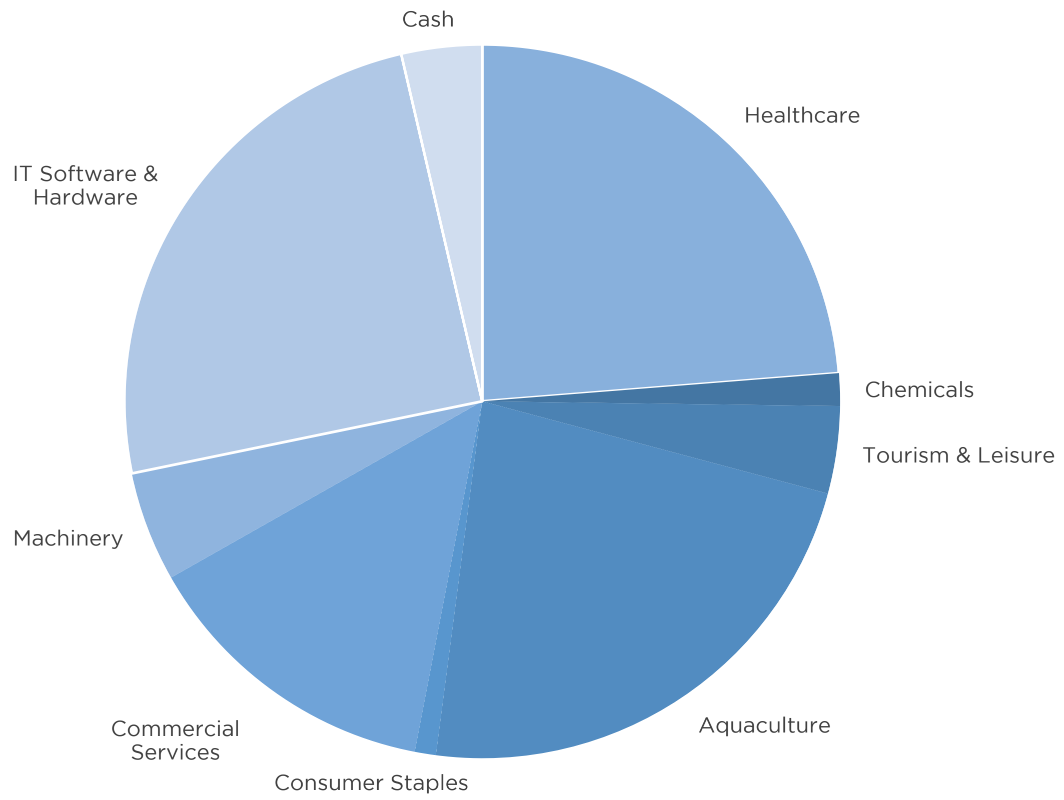
Dropsuite (DSE, +2%) had yet another very good quarter, with ARR up +35% on pcp and up +7% QoQ (constant currency), partly driven by the onboarding of 26 new direct and 231 indirect transacting partners. The Company continues to generate strong gross margins (~70%), positive cash flow and remains well-funded with $24.3m in cash. Given that DSE will now start to cycle the loss of a material (but low-ARPU) client from 1Q CY24 onwards, we expect its ARR growth rate to accelerate as we progress through this year.

IMR received a couple of key approvals during the month. Firstly, it obtained Medical Device Marketing Authorisation from the Saudi Food & Drug Authority and is now launching commercialisation efforts in that Country. The first system sale is expected there within six months, noting that Saudi Arabia performs nearly 50,000 cardiac ablation procedures per annum, so it represents a significant market opportunity for IMR. Secondly, IMR received approval from the (world-renowned) John Hopkins Hospital's Institutional Review Board for the commencement of its VISABL-AFL clinical trial, to commence in February. This trial will lead to FDA approval of IMR's products, noting that it already has CE Mark approval for atrial flutter applications, hence why it already has commercial operations in Europe and other markets such as the Middle East where CE Mark applies.

Finally, we note that 5GG delivered another breakeven quarter, with Gaming subscription revenue up +51% QoQ and Telco on-net subscriber installs up +24% QoQ for the six weeks following its 5G Fixed Wireless launch at the end of October, which bodes well for CY24.

Portfolio characteristics

We currently have ~96% of our capital invested in 14 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,

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Principal

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