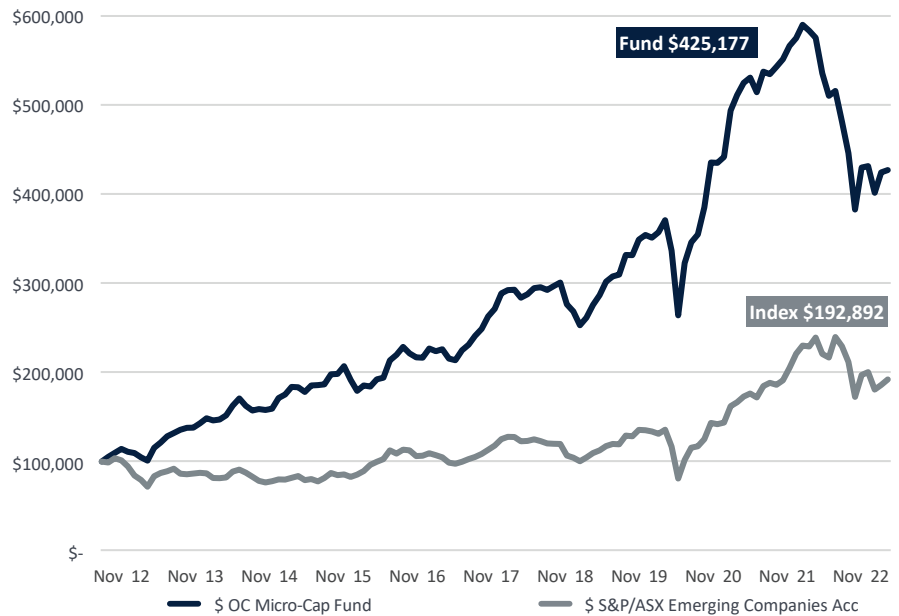


**0.6%** Fund up 0.6% for the month

**9.5%** Returned 9.5% p.a. for the past 5 years

We remain confident the Fund is well placed to deliver strong long-term returns

### Performance comparison of \$100,000 over 10 years\*



### Total returns

At 30 Nov 2022 <sup>1</sup>	1 mth %	3 mths %	1 yr %	3 yrs % p.a.	5 yrs % p.a.	10 yrs % p.a.	Incep. % p.a. (Nov 2003)
OC Micro-Cap	0.6	-1.0	-26.8	6.7	9.5	15.6	12.9
S&P/ASX Emerging Comp. Accum	3.3	-4.1	-16.2	12.9	10.3	6.8	6.2
<b>Outperformance</b>	<b>-2.7</b>	<b>3.1</b>	<b>-10.6</b>	<b>-6.1</b>	<b>-0.8</b>	<b>8.8</b>	<b>6.7</b>

Inception date for the Fund is 21/11/2003. Inception date for the Index is 31/12/2003. The performance reflects the performance of the OC Micro-Cap Fund since the change of strategy on 31 October 2016 and the performance of the OC Concentrated Equity Fund prior to that date. Performance is after fees applicable at the time. The total return performance figures quoted are historical, calculated using cum-distribution end-of-month hard-close mid-prices and do not allow for the effects of income tax or inflation.

### Performance review

Equity markets continued to recover in November after a softer than expected US CPI print and a dovish speech from Federal Reserve (the Fed) Chair Jerome Powell fuelled optimism that interest rates in the US may soon peak and that a protracted recession in the world's biggest economy can be avoided. The domestic small and micro-cap market cruised through a relatively benign AGM season with a resurgent resources sector (S&P/ASX Small Resources Accumulation Index up 11.6%) helping to drive the S&P/ASX Emerging Companies Accumulation Index up 3.3% for the month. The OC Micro-Cap Fund had a solid month, up 0.6%, which was behind the broader index due to our limited exposure to speculative resource stocks which drove the strong benchmark return.

**Aroa Biosurgery (ARX, +25.7%)** traded higher during month as investors began to price in tailwinds that the business ought to be experiencing. This optimism was confirmed when the company delivered a strong interim result (March year-end) and upgraded its earnings guidance at the end of November. ARX is a soft-tissue

regeneration company that develops, manufactures, sells and distributes medical and surgical products to improve healing in complex wounds and soft tissue reconstruction. Auckland based, ARX has multiple products in market (or in late stage development) and these products are developed from a proprietary technology platform being a novel extra-cellular matrix bio-material derived from ovine (sheep) forestomach. Some of the tailwinds that ARX is experiencing include reopening of its core hospital customer base in the US post COVID-19, ongoing penetration of hospitals through an expanding US based salesforce, broadening product portfolio, expanding gross margins and a weakening NZD (against sales into the US). ARX has \$45m net cash and is priced by the market at an undemanding market capitalisation of \$375m. We consider that this offers good value given its prospects for high growth, expanding margins and its large free cash flow generation potential. We have held ARX in the portfolio since its IPO, albeit we have taken the opportunity to trim our weighting into share price strength.

**Aspen Group (APZ, +10.4%)** rallied after providing the market with a strong 1H trading update and a conservative guide to the market for FY23 EPS and DPS, which were in line with our expectations. APZ is a relatively new position entered into by the micro-cap fund largely through a capital raise at \$1.58. APZ holds a range of assets across the residential property, caravan park, workforce accommodation and retirement sectors. APZ is led by Joint CEOs John Carter and David Dixon who each have over 30 years of property banking experience at various investment banks. John and David, who have an excellent track record of executing accretive acquisitions, are both highly aligned, owning a substantial amount of stock and have been executive directors over the past three years. In this time, the strategy has evolved to focus on affordable accommodation which attracts a \$400 weekly rent or \$400K purchase price. APZ has grown into this sector by making opportunistic acquisitions of distressed residential property assets below replacement value which are then refurbished and re-leased. As an example, APZ acquired a portfolio of 514 apartments in Perth in 2021 for \$55M which were 41% occupied generating \$0.7M in Net Operating Income (NOI). Over the last year, APZ has deployed \$20M in capital on refurbishments and this asset is now 98% occupied and generating \$4.1M in annual NOI. Post completion of the refurb programme, APZ expect this asset to generate a 9.8% gross yield on cost or 6.2% net yield on cost, which we see as highly attractive for the respective asset class.

We acquired our holding in APZ at a discount to Net Tangible Asset (NTA) backing which is based on NOI which is growing as refurbished units are re-let. These asset classes tend to have excess demand, limited supply and consequently rising rents.

**Pacific Smiles (PSQ, +10.3%)** finished higher after an eventful month for the company during which the largest shareholder and founder Alex Abrahams convened a general meeting to replace the directors of the company. Dr Abrahams proposes to improve utilisation and margins by reducing the organic roll out of new dental clinics and adding additional higher value procedures. Whilst there is merit to his view, we find it difficult to support his proposals given the proposed board lacks ASX listed experience and there is not an identified CEO. PSQ has been viewed by the market as a dental services business which has recently struggled to expand margins as it has been rolling out new clinics. Whilst the company generates organic growth as these new centres mature, there is a short-term impact to margins as these clinics generally make losses during their first year of operations. PSQ had materially increased the rate of new clinic roll outs during FY21 in order to secure quality shopping centre locations, which combined with the omicron COVID-19 strain, dragged on margins into FY22.

Following Dr Abrahams notice to convene a general meeting, PSQ provided a trading and strategy update to the market which showed solid recent trading and reiterated the FY23 earnings guidance. Furthermore, PSQ has elected to reduce the rate of organic roll out to approximately 10 centres per year which reflects shareholder concerns around margin impact and utilisation. We think the decelerated roll out and focus on utilisation is the correct strategy for the company to employ and have retained our holding. Should management execute on the plan, margins ought to track higher and we should see the benefit from earnings growth due to the maturation of centres. We will closely monitor the shareholder vote to replace the board which will take place on 19 December, although we do not expect it to be successful at this stage.

**City Chic Collective (CCX, -38.1%)** was down for the month after releasing a surprisingly negative trading update at their recent AGM. To recap, CCX is a predominantly online retailer of plus-size womens apparel in Australia, the USA and Europe. CCX over invested in inventory a year ago when supply chain challenges were most acute and the consumer was buoyant due to fiscal stimulus. Since this time, the global economic outlook, particularly in the USA and Europe, has deteriorated resulting in a 87% fall in the share price over the last 12 months (which we have largely avoided) and elevated short interest in the stock. Whilst the market was aware that CCX had been overstocked and would be required to discount heavily to clear inventory, the impact on margins for the first quarter was more negative than expected. For the quarter CCX experienced a revenue decline of 2% on pcp and 9% compression in gross margins driven by volatile demand in a heavy promotional environment in the northern hemisphere. By contrast, the southern hemisphere has delivered 10% growth, albeit against a prior year which was affected by lockdowns.

The market reaction was severe and today the share price ascribes a 'market valuation' for the ANZ business (which is still performing) and 'liquidation value' only to the northern hemisphere business for a large customer list and inventory. CCX is aiming to return to historical levels of gross margin over time as inventory levels normalise and macro pressures ease. Furthermore, shipping rates and fulfilment costs are expected to reduce as CCX consolidates its 3rd party logistics (3PL) providers to offset the rate card increases which CCX is currently experiencing from these providers due to labour, fuel and infrastructure price rises.

Whilst demand in the near term is likely to remain uncertain, CCX is making concerted efforts to reduce its overstocked inventory position. We believe the balance sheet is unlikely to require a capital raise and can emerge as a stronger business with a net cash balance sheet in

June 2023. At this point the company should trade at a more appropriate valuation reflecting a normalised earnings profile.

## Outlook

Global equity markets have shrugged aside aggressive central bank tightening and staged a remarkable recovery in recent months with the US Dow Jones Industrial Index briefly re-entering bull market territory (20% increase off its late September lows) in late November. The catalyst has been a growing view that inflationary pressures have now peaked in key economies and that central banks will soon cease their aggressive monetary tightening as the global economy slows and pricing pressures subside. Supporting this view, the US CPI printed at 7.7% in October, cooler than had been expected, although household staples such as shelter, food and energy remained among the largest contributors to consumer prices and are still rising at a historically fast pace. Whilst this optimistic scenario cannot be outright dismissed given that we are in uncharted territory, it is not one which we consider likely given that inflation is proving to be sticky, economic activity and job markets remain robust, and key central banks including the Fed and RBA continue to reiterate that rates need to rise further to bring inflation back to their respective target ranges. The lag effect of monetary policy means that both the US and the Australian economies, along with much of the Western world, are likely to slow considerably into calendar year 2023, with at least a shallow recession in the US still our base case assumption.

Earlier this month, the RBA delivered its eighth consecutive increase in the official cash rate at its final meeting of 2022. Interest rates in Australia have now gone from just 0.1% in early April to 3.1% in short order. On the inflation front, the headline CPI fell to 6.9% in October, well below market expectations (7.4%), although the relief is likely to prove temporary given that the October result is yet to fully reflect the impact of the recent floods on grocery prices, nor the latest surge in energy bills. Despite the rapid increase in rates this year, the RBA will likely continue hiking rates into the new year, a position reinforced by Philip Lowe in his post board meeting policy statement. Unemployment remains stubbornly low at 3.4%, a near 50-year low, and a solid household savings buffer leaves domestic consumers well positioned even allowing for near-term inflationary pressures, rising interest rates and a softening housing market. We are retaining a domestic bias in our portfolio, as we view the domestic economy as being better placed to avoid recession than key offshore economies including the US, UK and Europe.

The November AGM season offered plenty of insights

into the strength of the domestic consumer, which seems to be holding up relatively well, although management were much more guarded in providing forward guidance into the new year with the mood perhaps best described as cautious. Domestic retail was an area of unexpected strength in AGM commentary with a number of companies including Nick Scali, Harvey Norman, Accent Group and Super Retail Group all still reporting buoyant trading and limited impacts, as yet, from rising rates or falling house prices. The Black Friday sales period was reported as being strong across the board and expectations for the critical Christmas trading period is broadly upbeat. It was significantly more difficult to garner optimism on the outlook with very few companies offering forward guidance and most agreeing that it is very difficult to know what the trading environment will look like once the full force of mortgage rate increases hit the consumer hip pocket and as the negative implications of a falling housing market (wealth effect) flow through.

Other key callouts observed by the OC Investment team during the month include:

- Labour availability and wage inflation remain a key issue for many companies, with some relief expected as migration returns to our shores and as international travel resumes;
- Supply chain pressures are still an area of concern, although container freight costs have fallen sharply and are back to pre-pandemic levels. Lead times on production are also moderating meaning that inventory reduction is becoming a key focus for those companies who have built 'just in case' inventory buffers;
- Input cost pressures are creating margin headwinds for companies unable to offset them through price rises (e.g Collins Foods);
- Australian dollar weakness versus the US dollar (USD) means that importers (who pay for goods in USD) will need to further increase prices into a softening consumer environment or suffer margin pressure;
- Rate hikes have materially raised interest cost for companies with floating rate debt and, in many instances, we feel the sell-side is behind the curve in factoring this into their forward earnings forecasts.

Back in early October we added some risk to the portfolio, predominantly in the form of oversold growth stocks, which has helped the portfolio to rebound over the past few months. In particular, we have been selectively adding quality stocks (e.g. Aussie Broadband and PeopleIn Limited) with long-term growth prospects as they are sold down to attractive entry levels. That said, we are cautious on the outlook for equity market following the sharp rally as we enter the new year with rate hikes likely still to come and with the economy likely to start to slow. The Fund remains cashed up and is well

positioned to capitalise on the opportunity to purchase quality businesses at compelling prices in the coming months as the opportunities arise.

### Top 5 holdings<sup>#</sup>

Company	ASX code
Cedar Woods Properties	CWP
Propel Funeral	PFP
Peter Warren	PWR
Silk Logistics	SLH
Telix Pharmaceutical	TLX

<sup>#</sup>The top 5 portfolio holdings are in alphabetical order and may not be representative of current or future investments.

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<sup>\*</sup>The total return performance figures quoted are historical, calculated using hard-close end-of-month mid-prices and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. The performance is quoted net of all fees and expenses. The index does not incur these costs. This information is provided for general comparative purposes.

<sup>\*</sup>The performance comparison of \$100,000 over 10 years is for illustrative purposes only. All returns shown are based on Australian dollar figures. Past performance is not a reliable indicator of future performance. The total returns shown are prepared on an ongoing basis (i.e. they include all ongoing fees and expenses and assume reinvestment of all distributions). They do not take personal taxation into account. The comparison with the S&P/ASX Emerging Companies Accumulation Index is for comparative purposes only. Index returns do not allow for transactional, management, operational or tax costs. An index is not managed and investors cannot invest directly in an index.

Past performance is not a reliable indicator of future performance. Positive returns, which the OC Micro-Cap Fund (the Fund) is designed to provide, are different regarding risk and investment profile to index returns. A performance fee of 20.5% is accrued daily on any excess performance (after deducting the management fee) above the performance benchmark within a performance period. Any accrued performance fee will become payable if the Fund's return is positive at the end of the performance period. If the Fund's return is negative, any performance fee accrual will continue to be carried forward. The performance benchmark is the return of the S&P/ASX Emerging Companies Accumulation Index. The inception date of the S&P/ASX Emerging Companies Accumulation Index is 31 December 2003. This document is for general information purposes only and does not take into account the specific investment objectives, financial situation or particular needs of any specific reader. As such, before acting on any information contained in this article, readers should consider the suitability of the information for their needs. This may involve seeking advice from a qualified financial adviser. Copia Investment Partners Ltd (AFSL 229316, ABN 22 092 872 056) (Copia) is the issuer of the OC Micro-Cap Fund (ARSN 126 537 424). A current PDS is available from Copia located at Level 25, 360 Collins Street, Melbourne Vic 3000, by visiting [ocfunds.com.au](http://ocfunds.com.au), by calling 1800 442 129 (free call) or by emailing [clientservices@copiapartners.com.au](mailto:clientservices@copiapartners.com.au). A person should consider the PDS before deciding whether to acquire or continue to hold an interest in the Fund. Any opinions contained in this document are based on information available to Copia at the time and may be subject to change without notice. Copia is under no obligation to update or keep any information contained in this document current.