SPHERIA ASSET MANAGEMENT

Spheria Australian Microcap Fund

ARSN 611 819 651 | APIR WHT0066AU | mFund SPM01

Performance as at 30th June 2022

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a[3]
Fund[1]	-9.1%	-16.4%	2.8%	16.9%	12.2%	12.9%
Benchmark[2]	-13.1%	-20.4%	-19.5%	0.4%	5.1%	5.3%
Difference	4.0%	4.0%	22.3%	16.5%	7.1%	7.6%
Microcap Index[a]	-18.6%	-28.1%	-7.3%	13.1%	11.6%	9.8%

1 Spheria Australian Microcap Fund. Returns of the Fund are net of applicable fees, costs and taxes.
2 Benchmark is the S&P/ASX Small Ordinaries Accumulation Index.
3 Inception date is 16 May 2016. Past performance is not a reliable indicator of future performance. All p.a. returns are annualised.
a Microcap Index refers to S&P/ASX Emerging Companies Accumulation Index.

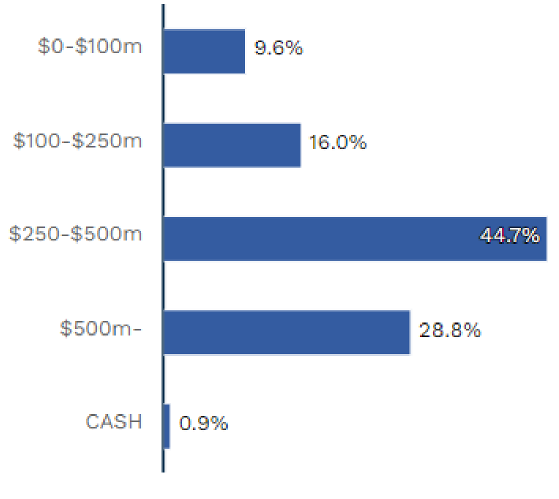
Overall Commentary

The Spheria Australian Microcap Fund returned -9.1% (after fees) during the month of June, outperforming the ASX Small Ordinaries Accumulation Index by 4.0%.

Top 5 Holdings

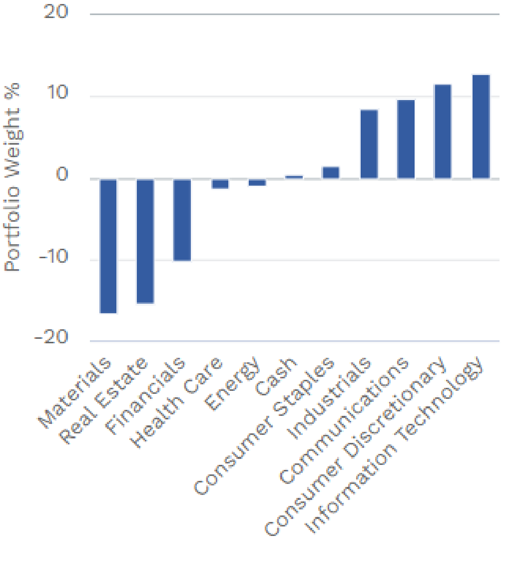
Company Name	% Portfolio
Vista Group International Limited	6.1
Nzme Limited	5.5
Reckon Limited	5.4
Michael Hill International Limited	5.3
Supply Network Limited	4.9
Top 5	27.2

Market Cap Bands



Source: Spheria Asset Management

Active Sector Exposure



Source: Spheria Asset Management

Markets

Legendary investor Warren Buffett is famous for saying "Only when the tide goes out do you discover who's been swimming naked."

We think this is an apt analogy of what has played out in the last six months as sharemarkets continued their sell-off into June, as global central banks continued to raise interest rates to counter inflationary pressures thus leading to a reassessment of risk and therein market prices for all asset classes. It's simple economics when demand is too strong relative to supply you get higher prices ("inflation") hence the need for central banks to raise interest rates to curtail demand. Unfortunately, central banks were far too accommodating for too long during the COVID-19 spell and the expectation is they are now likely, as per usual, to over-react the other way for too long. Markets do not like higher interest rates and the level of indebtedness across economies is alarming both in the context of government and households, thus servicing the interest bill will likely crimp demand via higher taxes and lower disposable income. Hence, the broad-based sell-off in sharemarkets and the more pronounced hit to consumer discretionary sectors and long duration assets – particularly those that are cash burning.

We have largely avoided the "cash burning crowd" as our process requires companies to be generating positive free cash flow (after all capital expenditures) or to do so with a high degree of certainty within a five-year time frame. The latter type being a very small component of our overall portfolios. Also, we have avoided companies where valuations were simply absurd – a manifestation of a long bull market and money printing when companies are trading on multiples of >50x and the market glibly thinks it's normal. This has protected our relative performance but is clearly no solace for those focused on absolute returns.

Many of our consumer exposed names have fallen significantly since the start of the year on the portent of weaker spend which has a feeling of inevitability, however, the duration and extent of which is unknown. Regardless, consumer exposed companies we own, in our view, are in a position of relative and absolute strength with respect to balance sheets (mostly net cash) and valuation multiples which were already incredibly low preceding this expected downturn, such that even if earnings halve the multiples will still be absolutely attractive e.g. Michael Hill (MHJ.ASX) would go from a multiple of 4x EV/EBIT to 8x and still have +$100m of net cash.

Major Contributors for the Month

Vista Group International (VGL.ASX) – rallied 10% in June after being heavily sold down on the back of potential weakness in its customer base (being cinemas) and then more broadly with the technology sector sell-off. The company announced at the end of May it had entered into a 10-year agreement to transition an existing major enterprise client in Latin America to its Cloud platform. The deal will involve annual subscription fees for which the company sees a material uplift to revenue and then to earnings as the product scales with new client wins and existing client transitions. VGL is the largest ERP software provider to cinema chains globally with over 50% market share by screen count.

Michael Hill International (MHJ.ASX) – rose slightly over the month in a falling market. MHJ is a stock we have held in the portfolio for several years and continue to like, despite it rallying over 350% from distressed COVID induced lows. The management team is executing well, driving further efficiencies in store and enhancing its online offering with the business experiencing eleven quarters of consecutive positive same store growth, despite significant interruptions over the last 2+ years. The company is actively looking for acquisition/s but in the absence of anything that meets its strict economic criteria, we believe a share buyback to be an efficient means of creating shareholder view given the current low trading multiple.

Reckon (RKN.ASX) – fell only 2% over June which outperformed the market selloff. In May, RKN rallied almost 50% driven by the announcement it had sold its Accountants Practice Management business for $100m. The share price held up over the month as the business confirmed the ACCC would not oppose the sale and that the all-cash sale of $100m was unconditional. This secures the cash for the company which is a significant win for shareholders as we anticipate they will distribute most of the proceeds (after tax) including any franking credits to shareholders. The remaining businesses are growing and have strong prospects although capital expenditures will be elevated in the Legal Practice Management division. Normalising for this elevated capex, we believe the remaining businesses are trading on only 5x EV/EBIT.

Major Detractors for the Month

Here, There & Everywhere (HT1.ASX) – declined over 26% in June as the media sector came under pressure due to expectations around an advertising recession. However, we do not believe the outlook to be so dire and conversations with management and more broadly suggest advertising spend is holding up well currently, this will change but is more than reflected in the trading multiple, in our opinion. Balance sheet debt is under control at <$100m (vs $70-80m of EBIT) and the company has a 25% stake in Soprano which is highly profitable and growing strongly, whilst its key competitors are cash burning, which we think plays out in Soprano's favour. HT1 is the No.1 rated metro radio network in Australia and recently acquired the largest regional player (Grant Broadcasters), to expand and complete its national presence and grow its digital offering, IHeartRadio.

Helloworld Travel (HLO.ASX) – fell almost 26% over the month on no news flow. The share price appears to have been caught in the broader market sell-off in June as the macroeconomic backdrop continues to weaken. We believe the demand for travel will mean revert and potentially over-revert after a multi-year hiatus due to government travel restrictions. The biggest issue for HLO and other travel agents is finding enough staff to meet the increased demand. With a strong balance sheet post the sale of its corporate travel business to CTD, HLO appears to be trading on less than 4x FY24 EV/EBIT when adjusting for surplus assets from the sale.

Hydration Pharmaceuticals (HPC.ASX) – share price nearly halved in June after a more pronounced sell-off of smaller micro-cap names and companies yet to be making an underlying profit. HPC owns the Hydralyte brand in the USA and Canada, and its management team were the architects of Hydrolyte's success in Australia. Whilst our process generally steers us away from loss making companies, we will make an exception for businesses where we can see a path to profitability and the management has a credible background. In April, the business reported they had achieved revenue growth of almost 120% in North America vs the prior corresponding period. Whilst annualised revenue is only US$8m, the total addressable market is large and the current growth rates significant. We believe management has the pedigree to repeat its success in the USA which could mean a significant payoff for early HPC shareholders in the long term.

Outlook & Strategy

It's grim for those companies that are burning cash and have little runway to raise money from previously benevolent shareholders, we feel there is a wave of insolvencies coming in this complex. This process though painful will ultimately be a healthy cleanse for the economy and the sharemarket, as many of these so-called "disrupters" were undermining returns for legitimate companies and had never formulated a path to an economic business model but were simply being propped up by cheap money from central banks. Those days feel over.

Whilst the economic backdrop will be difficult for our companies as revenues will be under pressure, we believe they will survive and likely thrive on the other side as the return equation improves – addition by subtraction really. Those investing on macro-economic themes are likely to find it difficult moving forward, we think bottom-up fundamental analysis will again shine and like the dot-com bust and the ensuing recession (shallower than expected in hindsight) it will be those portfolios that are biased to cash flows, solid balance sheets and sensible valuations that will generate the strongest returns for clients.

Platform Availability List

If a fund is not available on your preferred platform, please contact us. Please check with your platform for minimum investment requirements and fees.

Aegis	FNZ Group	MLC Navigator	PowerWrap
Asgard	HUB24	MLC Wrap	Praemium
BT Panorama	IOOF eXpand	Netwealth	Premium Choice
DPM	Macquarie Wrap	OneVue	Wealth02 uXchange

Spheria Australian Microcap Fund	
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Investment Objective	The Fund aims to outperform the S&P/ASX Small Ordinaries Accumulation Index over the medium to long term
Investing Universe	Primarily listed companies outside the top ASX 250 listed companies by market capitalisation and companies listed on the New Zealand Stock Exchange with an equivalent market capitalisation
Holdings	Generally 20-65 stocks
Distributions	Annually
Fees	1.35% p.a. management fee & 20% performance fee of the Fund's excess return versus its benchmark, net of the management fee
Cash	Up to 20% cash, typically 5% - 10%
Expected Turnover	20% - 40%
Style	Long only
APIR	WHT0066AU
Minimum Initial Investment	$25,000

Spheria Australian Microcap Fund

ARSN 611 819 651 | APIR WHT0066AU | mFund SPM01

Fund Ratings

Further Information

For more information, please contact Pinnacle Investment Management Limited on 1300 010 311 or email distribution@pinnacleinvestment.com

Disclaimer

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Link to the Target Market Determination
For historic TMD’s please contact Pinnacle client service Phone 1300 010 311 or Email service@pinnacleinvestment.com
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