Spheria Australian Microcap Fund

ARSN 611 819 651 | APIR WHT0066AU | mFund SPM01

Performance as 31 December 2022

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a[1]
Fund[2]	-4.4%	3.9%	-10.8%	15.2%	9.7%	13.0%
Benchmark[3]	-3.7%	7.5%	-18.4%	1.4%	2.9%	5.9%
Difference	-0.7%	-3.6%	7.5%	13.9%	6.8%	7.1%
Microcap Index[a]	-3.6%	2.6%	-22.5%	12.3%	8.2%	10.2%

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

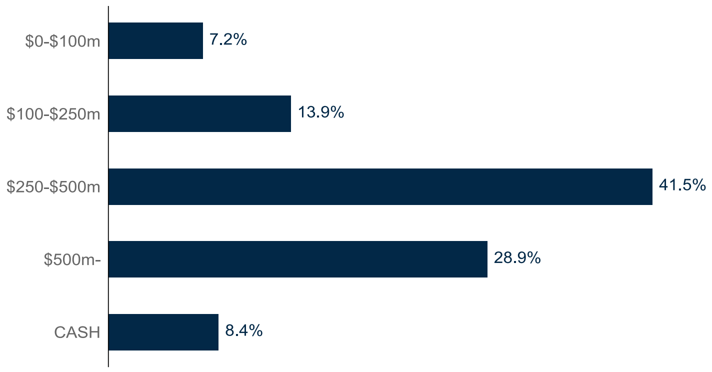
Overall Commentary

The Spheria Australian Microcap Fund returned -4.4% (after fees) during the month of December, underperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.7%.

Top 5 Holdings

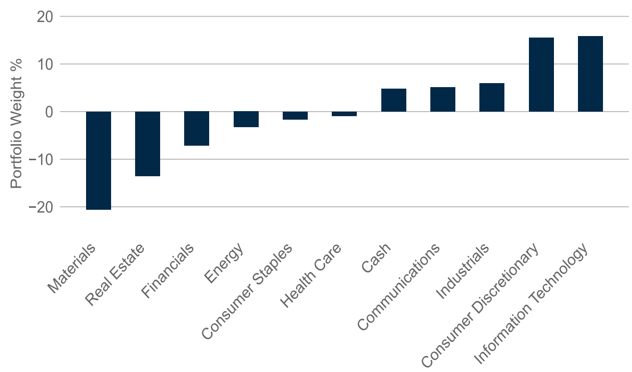
Company Name	% Portfolio
Nitro Software Limited	5.1
Supply Network Limited	4.5
Appen Limited	4.0
Mader Group Limited	4.0
Michael Hill International	3.9
Top 5	**21.6**

Market Cap Bands



Source: Spheria Asset Management

Active Sector Exposure



Source: Spheria Asset Management

Markets

The benchmark fell nearly 4% in December erasing most of the large gain made in November. A perfect storm of negative macro-economic factors continues to pummel asset prices with market participants praying for relief from Central Banks that are fixated with reining in rampant inflation (which they created mind you) by snuffing demand. Monetary policy is a blunt instrument – it will work in time – and we are beginning to see the impacts in the real world with a number of companies in various sectors downgrading profit expectations in the last few months. With a lot of negativity baked into valuations particularly at the "value" end of the market we feel the risk reward scenario is favourably skewed for long term investors, particularly if interest rates have peaked which feels likely given the unprecedented nature of the tightening in terms of speed and overall magnitude of increases relative to high levels of household debt.

Major Contributors for the month

Positive performance contributions from companies owned included:

Bravura Solutions (BVS.ASX) – rallied +10% in December continuing to rebound after its share price collapsed at the beginning of November after announcing a significant downgrade to profit expectations which will result in the company losing money in FY23. We had a relatively small position ahead of this update which we increased substantially in the ensuing share price falls. We do not expect this to be a quick turnaround given many years of mismanagement which will require a material realignment of the cost structure on a now smaller revenue base, however, the software is difficult to displace/replace which means the revenue is "sticky" and provides breathing space to effect necessary changes. Also, we calculate the company will have +$25m of net cash as at the December half year after restructuring charges and working capital imposts which we believe will provide sufficient liquidity to support the turnaround. BVS has now rallied nearly 50% from where we acquired the majority of our holding but still looks inexpensive on a through the cycle basis at about 4-5x EV/EBIT.

Nitro Software (NTO.ASX) – gained 5% outperforming the broader market as the bidding war between Alludo and Potentia carried over to December. We have discussed NTO in several commentaries after the company received proposals at $1.58 and later $1.80 from Potentia, followed by a $2 Board recommended offer from Alludo (a software company owned by KKR) in November. In December, Potentia matched the $2 bid, however, this was quickly countered by Alludo with an increase to $2.15. Post month end, both parties have lodged applications to the Takeover Panel alleging shortcomings in the opposite camp's takeover offers. The share price is trading at a slight premium to the highest bid from Alludo on the expectation that Potentia raises its offer to $2.15 or higher thus escalating the battle for control.

Universal (UNI.ASX) – rose over 3% in December on no obvious news. The company provided a trading update in November which revealed sales (excluding TRILLS, a recent acquisition) were up 40.2% vs the prior corresponding period. Noting the comparison in the prior period was impacted by lockdowns in NSW and Victoria the result was still positive in the current environment with many fearing a significant slowdown in consumer spending. Another positive was that YTD gross margins have improved which is in somewhat of a contrast to several other retailers locally and abroad which have seen gross margins fall recently as they look to discount to clear stock. Consistent with our investment thesis on UNI they have prided themselves on avoiding heavy discounting to maintain their brand perception and support gross margins. Whilst we acknowledge FY23 may be a challenging year for many retailers as higher inflation and interest rates potentially impact the consumer, we feel UNI is well placed to weather any slowdown. Their target customer is 18-24 years of age and tend to have more disposable income as they are less exposed to mortgages. UNI has a net cash balance sheet and is trading on ~7x EV/EBIT.

Major Detractors for the month

City Chic Collective (CCX.ASX) – continued to fall in December after the company provided another weak trading update with global YTD revenue (as at 18 December 2022) down 7% vs the prior period due to weaker than expected Black Friday/Cyber Monday sales. The weaker retail environment and excess inventory position has forced increased promotional activity which has resulted in further gross margin compression. The company is now expecting a small loss in 1H23. We do not expect this equation to improve in the short to medium term as the company works through elevated inventory. Of greater importance at this point is liquidity and transitioning the balance sheet from a net debt to net cash position which unfortunately is at the expense of group profitability. We are taking a longer-term view on this company and will support the business in the event of a capital call.

Adore Beauty (ABY.ASX) – is a relatively new position in the portfolio. The share price fell almost 38% in December as e-commerce players continued to come under selling pressure as consumers continued their shift back to bricks and mortar. Adore Beauty is a leading online beauty retailer in Australia offering over 11,000 third-party products. The company listed in late 2020 at $6.75 and has fallen considerably over the last two years to be around $1 now. The business now has over 800k active customers with ~60% of its revenue from its customer loyalty program. The company's market capitalization is now around $100m and it had nearly $30m of cash at 30 June 2022, which means its Enterprise Value (EV) is now a paltry $70-80m. The company generated positive free cash flow in FY22 unlike many of its peers.

Ainsworth Gaming (AGI.ASX) – fell almost 18% in December on no news. As discussed in last month's commentary AGI was one of the top contributors with the share price rallying 58% after the company revealed they expected 1H23 PBT to be approximately $18m compared to the $10m earned in 1H22, a significant increase from losses experienced in 2021. The company generated $45m of free cash flow (before tax) in FY22 and now sits on +$50m of cash (no debt) and has valuable property in Las Vegas (+$50m) and Florida (+$10m). The business is trading on about 6-7x EV/EBIT and is returning to growth under a new management team.

Outlook & Strategy

We are highly constructive on valuations for the companies in our portfolio and for the majority their financial strength, where there is balance sheet risk – for example CCX – we believe the position size appropriate given the range of scenarios. These factors provide us comfort that we are in a strong position to navigate a complex and an extremely challenging economic environment.

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 Funds 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

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Fund Ratings

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For more information, please contact Pinnacle Investment Management Limited on 1300 010 311

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Link to the Product Disclosure Statement
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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