SPHERIA ASSET MANAGEMENT

Spheria Australian Microcap Fund

ARSN 611 819 651 | APIR WHT0066AU | mFund SPM01

Performance as at 30 September 2023

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a[1]
Fund[2]	-4.7%	3.3%	12.6%	21.1%	11.2%	12.9%
Benchmark[3]	-4.0%	-1.9%	6.8%	2.6%	1.6%	5.2%
Difference	-0.6%	5.2%	5.8%	18.5%	9.6%	7.6%
Microcap Index[a]	-4.9%	-5.3%	-3.0%	7.4%	8.0%	8.3%

[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.

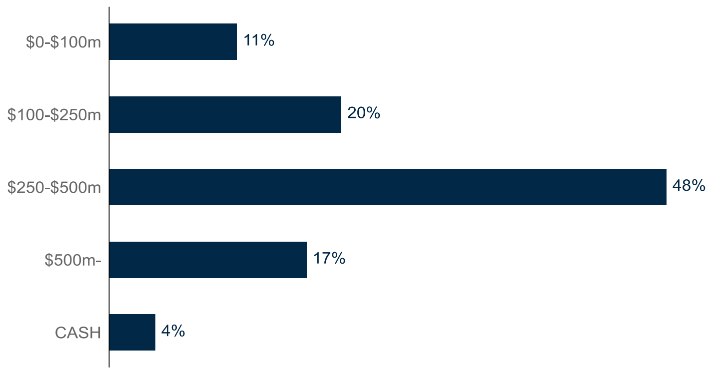
Overall Commentary

The Fund returned -4.7% (after fees) for the month of September, underperforming the S&P-ASX Small Ordinaries Accumulation Index by 0.6%.

Top 5 Holdings

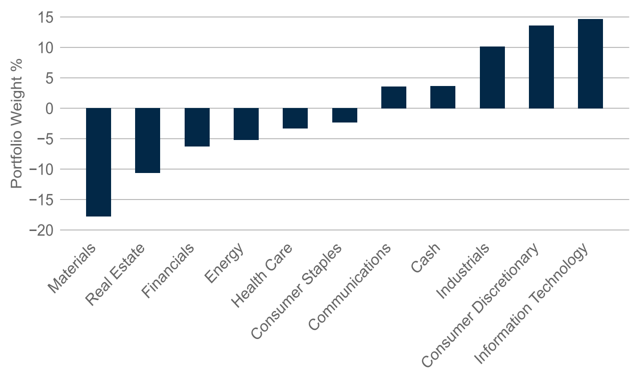
Company Name	% Portfolio
Supply Network Limited	5.0
Bravura Solutions Limited	4.4
Mader Group Limited	4.3
GWA Group Limited	4.2
Michael Hill International Limited	4.1
Top 5	**22.0**

Market Cap Bands



Source: Spheria Asset Management

Active Sector Exposure



Source: Spheria Asset Management

Markets

Many parts of the sharemarket especially the smaller company end have entered something resembling the "Twilight Zone" where unusual phenomena are so frequent that nothing really surprises us anymore. Case in point being the extreme disconnect in valuations between "growth" and "value" companies where the definition of each is simply a gauge of popularity or unpopularity in the case of value. Money is also clearly exiting the smaller end whether it be a flight to safety or industry funds exiting mandates given the marginal incremental contribution to performance given their increased size. The selling in certain names and the lack of risk appetite has meant extremely large drawdowns for anything resembling a negative earnings delta. This has been accentuated in anything that has debt regardless of whether the company's cash flow can support that debt. We have been caught in several of these situations across the portfolios and even when this equation has been addressed via capital raisings and/or asset sales the stigma has continued to weigh on the company's valuation and share price despite the sharp reduction in risk. Interestingly, earlier in the year we entered Bravura Solutions (BVS) a little early, only for it to have a near death experience where we were a key party to a significant recapitalisation at 40c. Subsequent to the raise the company inexplicably traded down to 29c. Since that time, we were heavily involved in re-working the board and ultimately the senior management team and the BVS share price has more than doubled from the bottom to trade in excess of 70c (at the time of writing). We feel several of our names are in a similar position but are still early in that recovery cycle.

Major Contributors to Performance

Over the month the largest contributors to performance were from overweight positions in Regis Healthcare (REG.ASX, +48bps), Horizon Oil (HZN.ASX, +38bps), and Reckon (RKN.ASX, +35bps).

Regis Healthcare (REG.ASX) share price rose over 9% in September outperforming the market on no new news. The company announced their financial year results at the end of August which showed averaged occupancy had improved from ~89% to 91.5% supported by a rebound in demand and a constrained supply environment. We expect this backdrop to continue over the short to medium term given the lack of new supply coming into the market, which should support occupancy and earnings for REG. In addition to this, the age care sector is being supported by additional government funding coming off the back of a recent industry review which highlighted both a lack of profitablity for aged care centers as well as inadequate care and support for residents. The new funding model is based on recouping cost inflation which will provide greater predictability for industry participants, in conjunction with improved occupancy this will drive better profitability for the industry and potentially disproportionately so for REG which has higher quality portfolio positioned in better socio-economic areas.

Horizon Oil (HZN.ASX) share price rose over 12% in September on the back of a strengthening oil price. For those not familiar with HZN, it has substantial interests in two conventional oil fields. The larger one being in the Beibu Gulf (off China) which has produced around 10k barrels of oil per day (bopd) on a gross basis for the last ten years and is forecast to do so for at least a further six years. The other being Maari that is off New Zealand and has produced around 5k bopd which has at least another 4 years of production at or around these levels. When we first acquired our position in HZN about 7 years ago it was trading around 4c and facing numerous issues including too much debt and serious corruption allegations in respect of its PNG gas assets, which were subsequently divested. It is now trading at 18c and has returned over $150m (9.5cps) of cash to shareholders over the last three years.

Major Detractors from Performance

The largest detractors from performance included overweight positions in Redbubble (RBL.ASX, -72bps), Adore Beauty (ABY.ASX, -69bps) and Praemium (PPS.ASX, -55bps).

Redbubble (RBL.ASX, -72bps) share price fell 24% in September on nothing of note. During risk off periods, micro-cap names can be significantly oversold due to general liquidity in the market, and this appears to be the case for RBL. It has had a tough 18 months, as the share price tumbled off the COVID highs as consumer spending patterns changed and revenue for the business moderated. The significant sell off created an opportunity for the Fund to initiate a position. Despite the company generating a loss last year, the group still had ~$470m of revenue and initiated a total cost out of $33-$40m to return the business back to profitability. The group achieved a neutral cash flow in July 2023 after the cost out in a seasonally weaker month which bodes well for FY24 and beyond.

Adore Beauty (ABY.ASX, -69bps) share price fell almost 25% in September on no company specific news. Not too dissimilar to Redbubble the share price has been caught up in the micro-cap sector downdraft and more specially consumer discretionary weakness. Revenue fell ~10% in FY23 from COVID highs of FY22 and earnings have retraced with the share price collapsing almost 90% since it IPO'd in late 2020. The Fund has only recently entered the name given the significant pull back in share price. Adore is the leading pure play online beauty retailer in Australia and has a loyal customer base with over 75% of their revenues being generated from returning customers. The business has a net cash balance sheet of ~$28m with a market-cap of $70.8m (at the time of writing) and assuming it can generate a 3% EBITA margin at mid-cycle it is trading on ~5x EV/EBITA.

Outlook & Strategy Going Forward

We feel our portfolio is well balanced between companies that are trading and executing well and are relatively popular and those that are in the throes of turnaround or recovering from a challenging experience. Given past experiences, we feel that the good companies where valuations are very compressed (A1N, ABY, RBL, CCX) trading at share prices that feel very uncomfortable is where the most returns tend to be had. In the meantime, our performance is being supported by businesses like SNL, MAD, MHJ, HZN that are trading well from an economic perspective and are not ridiculously expensive.

Platform Availability List

The Spheria Australian Microcap Fund is available on the below platforms. Platforms provide investors with consolidated and centralised reporting (including administration, tax, and distribution) by bundling together a range of managed funds as one single product

Acclaim Wealth	HUB24	MLC Navigator	Praemium
Asgard	Insignia Expand	MLC Wrap	Premium Choice
BT Panorama	IOOF Portfolio Service	Netwealth	
DASH	Macquarie Wrap	OneVue	
DPM	mFund	PowerWrap (IDPS only)	

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

Spheria Australian Microcap Fund

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Fund Ratings

Contact Us

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

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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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