DMX
ASSET MANAGEMENT

DMX Capital Partners Limited

Investing in the most compelling small and micro-cap value opportunities

DMX Capital Partners Limited

January 2020 – Shareholder Update

An investment company managed by:
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DMXCP directors: Roger Collison
Dean Morel
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Opening NAV (1 January 2020) [1,2]	**$1.9262**
Closing NAV (31 January 2020) [1,2]	**$1.9712**
Fund size (gross assets)	$9m
% cash held - month end [4]	19%
Gearing	nil

1 month return	**2.33%**
3 month return	5.55%
12 month return	27.76%
3 year return (p.a.)	8.69%
Since inception (4 years, 10 months) (p.a.)*	25.13%

*DMXCP Share price = Closing NAV (**$1.9712**), being: Share portfolio value + cash – fees payable – tax payable + franking credits*
**Return since inception (1 April 2015) includes 24c of dividends and franking credits paid*

Dear Shareholder,

DMXCP's NAV increased 2.33% (after all accrued fees and expenses) for January 2019. The NAV as at 31 January 2020 was **$1.9712**, compared to **$1.9262** as at 31 December 2019.

For the first seven months of the FY20 financial year, DMXCP's NAV has increased 21.02% (after all fees).

ASX indices were strong during the month. The All Ordinaries was up 4.68% in January while the ASX Small Ordinaries Index increased 3.92%. The XEC Emerging Companies Index increased 3.53%.

January commentary

It was a busy start to the year for the portfolio with several positive updates to holdings that supported share price increases (as opposed to stocks rising on no news or hype). Notable developments, including important acquisitions for Easton Investments (ASX:EAS) and PTB Group (ASX:PTB), are discussed below. However, we have also reduced our weighting to several stocks in the portfolio where we feel that recent share price increases have resulted in heightened expectations (and therefore risk) which may be challenging for stocks to deliver. Our cash levels increased from 14% to 19% during the month. Key contributors were Kip McGrath Education Centres (ASX:KME), Stream Group (ASX:SGO) and Urbanise (ASX:UBN). Detractors included Sequioa (ASX:SEQ) as well as some smaller positions.

While the broader market continues to perform strongly, we feel it continues to move ahead of fundamentals. We noted a number of downgrades through the month across a range of sectors, with a far smaller number of upgrades observed. We expect to see plenty of volatility upon reporting, as inflated share prices adjust to the reality of muted earnings growth. Uncertainty around the impacts of the Australian bush fires and Coronavirus will also subdue earnings outlooks for many companies. The market is currently trading on ~18x PE, with earnings growth of less than 4% expected.

Good investing ultimately comes down to sound decision making in relation to buying, holding and selling (with some good luck along the way!). We continue to have frequent, robust discussions amongst the team on the merits of every stock in the portfolio, assessing the various potential upside and downside scenarios and valuation implications, to ensure that weightings are appropriate, and the portfolio is managed in a disciplined manner. This is particularly the case leading into reporting season.

Key developments during the month for our portfolio holdings:

Easton Investments Limited (ASX:EAS)

EAS announced the acquisition of an initial 60% of TaxBanter, a leading national provider of online and in house training to the accounting profession (https://taxbanter.com.au/). The acquisition was priced at 4.2x forecast EBITA and is expected to contribute $1.1m EBITA to EAS's FY21 earnings. TaxBanter will complement EAS's fast growing Knowledge Shop training business. At its AGM in November, EAS advised that its Knowledge Shop training revenues were up 27% in the four months to October 2019. This represents organic growth, and primarily driven by an increase in training hours to the wealth sector where Continuing Professional Development (CPD) training requirements are resulting in significantly increased demand. Kaplan and EAS are now the key players offering financial advisor CPD training solutions in this post royal commission environment where training and compliance is becoming a critical focus.

Together, the two businesses (TaxBanter and Knowledge Shop) are expected to contribute $10m of generally recurring annual training revenues (online and face to face) at high margins. This training business will become the largest contributor to EAS's profits. There is potential for corporate activity here if EAS decide to dispose of its traditional accounting and financial advisory businesses, to focus on the high growth, higher quality revenue opportunities in the training space. Alternatively, a training business with $10m in recurring revenue, which is increasingly moving from lower margin, face-to-face training, to higher margin, online training, is likely to have significant corporate appeal to a trade buyer.

EAS is trading at less than 10x PE. Its share price trades at the same level it did five years ago, yet it is a far more robust, diversified business today, than any time in its past.

PTB Group (ASX:PTB)

We initiated a small position in PTB, an aircraft engine maintenance and service provider, late last year. We were attracted to PTB due to its market leading position (in the Pacific) and its high margin, recurring, maintenance revenues that it captures. Towards the end of January, PTB announced the acquisition of a similar business, Prime Turbines, which operates in the US. PTB is generally restricted to operating in the Asia Pacific region based on current approvals. Prime's strong accreditations will therefore provide an avenue for additional growth within, and beyond, the US markets.

This is a transformational acquisition for PTB – doubling the size of its business, while also providing a strong platform for PTB to continue to grow. The Prime business is well known to PTB and has 30-plus years of expertise on major turboprop and turboshaft engine platforms.

In addition, as the current demand for PTB services in its Brisbane workshop exceeds workshop capacity, PTB is currently required to outsource excess work to US workshops. There is approximately $1.5m of pre-tax margin currently forgone, which will now be captured within the PTB Group. As a result of this margin capture, the acquisition will be highly accretive to PTB (23.7%). At the offer price of 69c, the company was being priced on less than 10x PE.

	PTB Actual FY 2019	Prime Turbines Pro Forma Run Rate	Combined	Additional Margin Capture	Combined including Additional Margin Capture
Revenue	$51.5M	$47.3M	$98.8M	$0.0M	$98.8M
EBITDA	$8.6M	$5.9M	$14.5M	$1.5M	$16.0M
NPBT	$5.6M	$4.6M	$10.2M	$1.5M	$11.7M
NPAT	$4.0M	$3.3M	$7.3M	$1.1M	$8.4M
Accretion in Earnings per Share Post Acquisition			8.0%		23.7%

Source: PTB's ASX Presentation dated 31 January 2020

The institutional placement to fund the acquisition was extremely well bid, and we received a small allocation from our bid. The placement is to be followed by an underwritten rights issue. With the offer price at 69c and share price (ex-dividend and ex-entitlement) currently at ~90c, we will be taking up our entitlements, while we have also agreed to sub underwrite a portion ($200k) of any shortfall in the entitlements issue.

UCW Limited (ASX:UCW)

Vocational and higher education company UCW reported one of the standout FY19 results in August 2019. At the time, UCW noted the momentum had continued into the start of FY20, with enrollments for its Australian Learning Group (ALG) subsidiary in early FY20 up 40%. This momentum was confirmed when UCW provided a market update in January.

ALG is expected to record 1H20 revenue of ~$9.3m (+35% on 1H19) while UCW's higher education subsidiary Ikon is expected to record 1H20 revenue of ~$3.3m (+43% on 1H19). Highlighting the operating leverage in the business, ALG is expecting EBITDA of ~$1.1m (from nil in 1H19) while Ikon is forecasting EBITDA of ~$0.5m (+400% on 1H19).

The business is inherently seasonal, with ALG, and particularly Ikon's revenue and EBITDA expected to be higher in the second half of FY20 compared to the first half. As a result, UCW is expected to report record consolidated revenue and EBITDA for the full year. There are a number of initiatives being undertaken to further drive growth, including increasing capacity, and a new Bachelor of Early Childhood Education Course that UCW is working towards achieving accreditation for.

It wasn't all positive however, as UCW has decided to write down its 25% investment in the underperforming Gradability to zero. With the write-down behind it, we look forward to positive underlying momentum coming through in future results. The company's exposure to China/Hong Kong students remains low at ~1.5%, and the Coronavirus is not expected to have any material short term impact on the business.

Kip McGrath Education Centres Limited (ASX:KME)

The share price of the portfolio's largest position tutoring company Kip McGrath performed strongly during the month. Following a query by the ASX to the price rise, KME noted that they had been approached by parties interested in potentially acquiring the business, and they are considering a number of strategic options including being currently engaged in preliminary discussions on a number of these approaches. We are aware of participants in the space with pure on-line operating models, who might find the Kip McGrath student network and IP attractive

It will be interesting to see what (if anything) eventuates from this current interest.

KME is a well led, strong performing, market leading brand with a global opportunity operating in a sector with some strong tailwinds– from our perspective, it is not surprising parties see interested in the business.

Appendix 4C Quarterly updates

Several of the smaller companies in the portfolio provided their second quarter (1 October 2019 to 31 December 2019) cash flow reports through January. We discuss three of these companies below.

Tambla Limited (ASX:TBL)

Workplace software company TBL reported a strong December quarter for 2019. TBL (which provides workforce payroll compliance, rostering, costing & award interpretation solutions) achieved cash receipts of $3.1m, generating net cash from operating activities for the quarter (inclusive of a $600k R&D rebate) of $1m, and $1.3m for the year. Pleasingly, TBL highlighted growing overseas interest in its products. After announcing its first US customer for its new PayCE SAAS product in the previous quarter, TBL has now secured six North American customers. As an 'out of the box' SAAS product, PayCE has much shorter sales and implementation cycles. This recent offshore validation provides encouraging evidence that TBL's solutions are exportable and scalable globally. TBL uses a distribution partner, Canadian software company Alayacare, to sell into North America, so it is pleasing to see this partnership having some success. We see continued offshore growth as a reason for the market to look at TBL more positively.

Domestically, TBL strengthened its presence in the government sector winning a new local government customer, while also confirming that its business development pipeline continues to build. Continued work force casualisation, particularly in areas of aged care, healthcare, retail and hospitality, is a strong tail wind here for TBL's solutions. TBL continues to invest in R&D and in business processes, as it focusses on becoming a more sophisticated and robust business. An example of this is TBL's new support desk which went live during the quarter, and which now provides live 24/7 global customer support for TBL's product suite.

Managing Director Chris Fydler commented: *"The December Quarter was another period of steady delivery for Tambla and we were pleased to round out the year with the fourth consecutive operating cash flow quarter.*

A key objective has been to enhance our suite of products and this remains an ongoing focus as it underpins our growing base of stable recurring revenue streams. The delivery of the Global Customer Support Desk was a key initiative for the Company and will help us maintain high retention rates and strengthen our business development initiatives.

As we enter CY2020, it is pleasing to note that our business development pipeline continues to strengthen and this bodes well for the year ahead. We look forward to reporting full year audited results in February."

TBL generates annual recurring revenue of ~$7m, is well managed, has high customer retention (95%), a growing global customer base (200 customers in total with over 2m rostered end users) and a growing distribution network. With a market cap of $8m, we consider it represents an attractive investment opportunity.

Aeeris Limited (ASX:AER)

AER, the geospatial data business, reported a cash flow positive quarter of $12k and also delivered a cash flow positive half year. AER maps, tracks, monitors and communicates severe weather events to its corporate and government clients, so has had a busy time of late. AER noted that the duration and intensity of the recent emergencies have been unprecedented in its operational history.

Pleasingly, AER advised that it was able to comfortably cope with the increased demands on its services. In addition, as a result of the extreme weather, AER has received a record number of enquiries for its services, which are expected to convert to annuity revenues over the coming months.

With a market cap of $7.5m, 95% recurring income and 99% customer retention, and ownership of unique and powerful data, AER continues to screen attractively at 3x ARR. It represents a sound, well managed, cash-flow positive, technology exposure to climate change scenarios and extreme weather and environmental events. AER's challenge is now to capitalize on its opportunity in-front of it, and to accelerate growth. It has noted it expects a strong second half, so we hope to see progress of this sales growth in the coming months.

Mr. Kerry Plowright, Chairman of Aeeris, said; "In an environment of unrelenting risk to life, the need for diligence and direct support of our customers has never been so important. Despite the massive increase in peril, the performance of EWN systems, staff and management was exemplary.

Chant West Limited (ASX:CWL)

CWL reported operating cash flow of $1m for the quarter and a cash balance at 31 December 2019 of $4m. With a market cap of $8m, this implies an enterprise value of $4m. CWL operates two profitable businesses. Firstly, Chant West, which owns proprietary software tools that help industry professionals compare products and financial planners advise their clients on superannuation matters. It is a high-quality business with about 85% of revenue being recurring, subscription based.

The second business is Enzumo, a consultancy business which conducts in-depth analysis of financial planning businesses and creates tailored technology solutions to help them operate more efficiently and compliantly. There was a concern that this business would be impacted by the recent disruption to the financial planning space. For the first time, in the quarterly, CWL has articulated the growth potential of Enzumo, noting that the growth experienced in FY19 has continued into FY20. Further evidence of Enzumo's momentum is its recent engagement to provide strategic consulting services to Intelliflo Ltd, the UK's leading financial adviser software provider, as they prepare to enter the Australian market.

Group update

Both operating businesses achieved a positive EBITDA in the December quarter and the half-year. The Group's strong cash position ensures we are well placed to navigate the structural changes in the industry and move quickly to capitalise on opportunities such as Intelliflo. We anticipate a further period of M&A activity in the financial services sector during 2020. The Company will continue to utilise its strong financial position to accelerate growth in both Chant West and Enzumo.

We are top 10 shareholders in each of these companies (AER, TBL and CWL). They are not sexy 'hyper' growth companies, so do struggle to attract much investor interest. We like them however, as they each have a solid core of high quality, long term, customers generating recurring revenues, and a strong pipeline of new business opportunities. Their Management teams are sensible and have a strong track record of being prudent managers of shareholder funds and making sound strategic decisions. It is not a surprise therefore, that each of these companies are consistently cash flow positive, despite all being small companies with market caps below $10m.

The three businesses have done the hard work to get to the critical point of sustainable profitability, and have proven that they have a profitable operating model. The challenge is now to grow revenues at a faster rate which will attract broader market interest. A growing, profitable company with a very low market cap that is able to generate operating leverage we consider represents a very powerful re-rate opportunity.

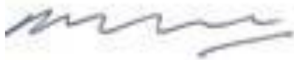
Accordingly, we believe these three companies provide some strong long term upside to the portfolio, as their respective management teams quietly continue to build them into bigger businesses. Meanwhile, we continue to be patient with our positions, and we would be happy to support them with further capital should an appropriate opportunity rise.

For further updates and news on portfolio holdings, please visit us on twitter or go to our blog.

Again, thank you for your trust, support, and patience as we continue to build and manage a portfolio of interesting, under-valued, under the radar opportunities in a disciplined and well structured manner. If you would like to discuss either initiating an investment or topping up your holding at this prospective time, please do feel welcome to contact Steve McCarthy on 0403 869 632 or email steven.mccarthy@dmxcorporation.com.au at any time.

We look forward to reporting to you again in early March.

Kind regards



Roger Collison	Steven McCarthy	Chris Steptoe
Chairman	*Portfolio Manager*	*Research Analyst*

Note 1: Net asset value (NAV) is after all tax accruals but includes an estimate of franking credits available. Refer note 5, unaudited
Note 2: Unaudited result
Note 3: All DMXCP disclosed returns include the payment of dividends and franking credits
Note 4: Excludes cash received during the month for the application of new DMXCP shares to be issued
Note 5: Franking credits per share are franking credits arising from dividends received and for tax paid or payable on realised portfolio gains

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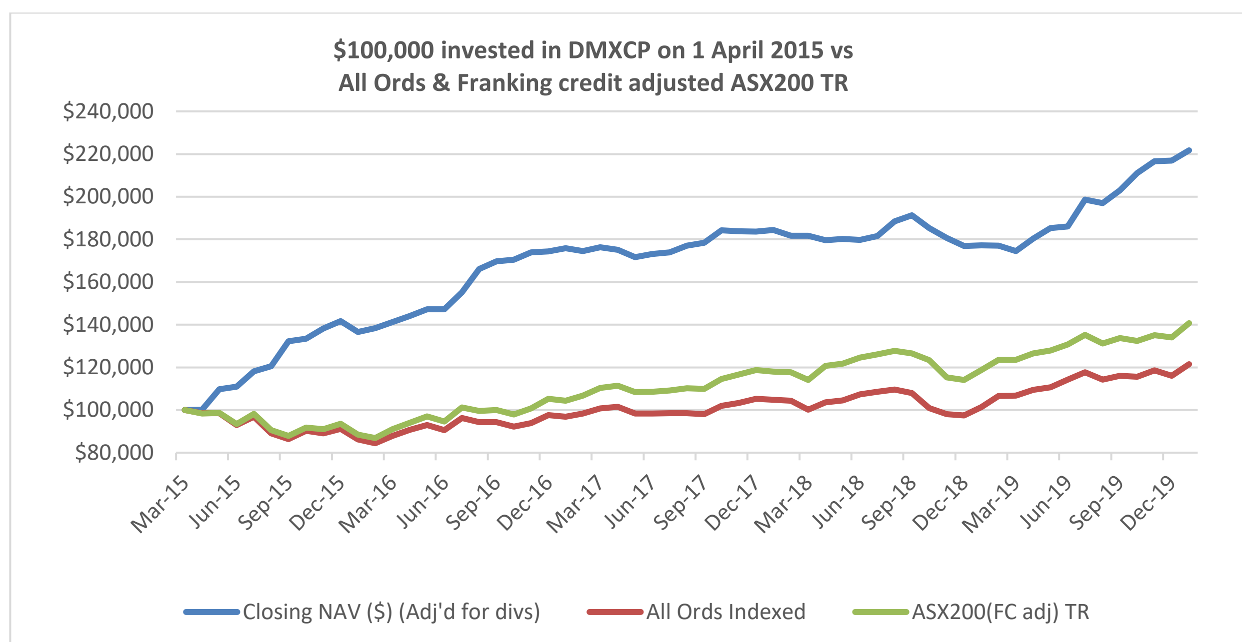
Appendix 1: Performance

Monthly DMXCP Net asset value (share-price) returns (after fees) since inception (April 2015) [(3)] (%):

Month	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	All Ords
2015	n/a	n/a	n/a	+0.201	+9.448	+1.104	+6.524	+1.971	+9.711	+0.958	+3.568	+2.470	**+41.62**	**-8.83**
2016	-3.590	+1.323	+2.049	+2.045	+2.143	+0.020	+5.389	+7.056	+2.156	+1.058	+1.520	+0.321	**+23.10**	**+7.01**
2017	+0.885	-0.816	+1.790	-0.741	-1.990	+0.210	+1.071	+1.208	+0.822	+3.494	-0.267	-0.055	**+5.54**	**+7.83**
2018	+0.445	-1.625	+0.008	-1.173	+0.310	-0.211	+1.017	+4.112	+1.604	-3.438	-2.827	-2.257	**-3.66**	**-7.24**
2019	+0.122	-0.010	-1.624	+3.754	+3.014	+0.418	+7.482	-0.889	+3.279	+4.567	+2.997	**+0.140**	**+25.10**	**+19.02**
2020	+2.33												**+2.33**	**+4.68**

The following chart illustrates the return from investing $100,000 in the fund (including dividends and attached franking credits) since inception (April 2015). DMXCP is an absolute return fund, focused on generating positive absolute returns over the medium to long term



Appendix 2: Portfolio Sector classification