DMX Capital Partners Limited

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

DMX Capital Partners Limited

October 2020 – Shareholder Update

An investment company managed by:
DMX Asset Management Limited
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DMXCP directors: Roger Collison
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Opening NAV (1 October 2020) [1,2]	**$2.1028**
Closing NAV (31 October 2020) [1,2]	**$2.3362**
Fund size (gross assets)	$13.5m
Gearing	nil
% cash held - month end [4]	17%

1-month return	11.10%
3-month return	31.13%
12-month return	34.07%
3-year return (CAGR p.a.)	15.52%
Since inception (*5 years, 7 months*) (CAGR p.a.)	21.17%

*DMXCP Share price = Closing NAV (**$2.3362**), being: Share portfolio value + cash – fees payable – tax payable + franking credits*
Returns include dividends reinvested and franking credits paid. Since inception 41c of dividends & franking credits have been declared

Dear Shareholder,

DMXCP's NAV increased 11.10% (after all accrued performance and management fees and expenses) for October 2020. The NAV as at 31 October 2020 was **$2.3362**, compared to $2.1028 (ex-dividend) as at 30 September 2020. The 2020 dividend of 12c plus franking credits, will be paid on or about 20 November 2020.

DMXCP has returned 29.66% for the calendar year to date (since 1 January 2020), and 40.13% for the financial year to date (since 1 July 2020) (after all accrued performance and management fees and expenses).

All indices were broadly stronger during the month, with the All Ordinaries up 2.06%, while the ASX Small Ordinaries Index increased 0.33% and the XEC Emerging Companies Index was up 1.27%.

October developments

October once again saw positive developments and encouraging trading updates across our portfolio. A number of portfolio companies reported first quarter revenue and profit results significantly ahead of the same quarter last year.

A key contributor to the performance this month was AVA Risk Group (ASX:**AVA**). In previous monthly reports we had talked about the strong start to the year that AVA was experiencing. This was confirmed when AVA announced a **73%** increase in 1Q21 revenue to $17m, while 1Q21 EBITDA improved by **522%** to $7.7m. In relation to its emerging fiber technology, AVA noted increasing activity in relation to its assurance sensing solutions for monitoring power cables and roads infrastructure. AVA again highlighted the strong commercial interest in its conveyor health fiber monitoring solution (Aura IQ) with multiple trials completed and/or underway. We see the initial Aura IQ sale as a significant potential near term catalyst for AVA.

Easton Investments (ASX:**EAS**) saw its share price increase 30% after it announced a $13m placement to ASX listed HUB24 (ASX:**HUB**) at a 38% *premium* to its market price. We have consistently expressed the view that EAS was materially undervalued, as it traded on a sub 10x PE multiple and has been growing its recurring revenue streams and profit over several years. The placement to HUB at a pleasing premium validates this view.

Other pleasing news-flow during the month included:

- Shavershop (ASX:**SSG**) delivered **20%** growth in sales in 1Q21 to $49.1m, with online sales increasing by 192%. Online sales now represent over 32% of total sales (1Q20: 13%). The strong sales growth was accompanied by healthy gross profit margins and ongoing cost control, leading to unaudited NPAT of $4.9m in Q1 up **185%**.

- Australian Family Lawyers (ASX**:AFL**) achieved revenue growth in 1Q21 of **34%** (to $2.4m) while underlying EBITDA for the quarter was up **130%** to $0.8m. AFL has a strong pipeline of organic, lateral hire and acquisition growth opportunities currently under review, so FY21 is shaping up to be a very strong year.

- Janison Education Limited (ASX:**JAN**) reported revenue of $7.8m for 1Q 21 (up **53**%). Recurring revenue from its Assessments division grew 29%. Gross Margin improved to 50% (up +3.4%). EBITDA for the quarter was $1.5m (up **425%).** $2.3m positive operating cash flow resulted in $12m cash on hand as at 30 September 2020.

Portfolio comments

Despite the uplift in our portfolio, and markets more generally, over recent months, we remain enthused about the value and opportunities within our portfolio, and the potential for these to drive continued respectable returns over time. To help understand our view here, it is useful to firstly provide some of our thoughts behind our portfolio construction.

We are desirous (and proud) of being supportive long-term orientated shareholders of our core holdings, with an ability to act with patience and conviction as our thesis plays out. But at the same time, given the opportunity cost, it is not ideal to have a portfolio heavily weighted to large sized long term positions where we are having to wait patiently for those positions to be 'discovered' by the market. Accordingly, we are also particularly focused on ensuring that the portfolio remains 'fresh', and at any point in time, offers an attractive risk/reward profile which also has potential for significant near-term upside.

To achieve 'balance' between these two competing long term and short term perspectives, we look to recycle the proceeds from selling/reducing positions that we consider to be significantly over-bought, or which have become over-weight in our portfolio, into new positions that have superior risk/return profiles. We also, of course, look to continue to add to existing holdings that represent compelling value.

In recent months, with some of our long-term positions experiencing significant market re-ratings, we have been able to reduce some of our previously larger holdings (the likes of CWL and AVA). Capital has been freed up to rotate into new opportunities that have not yet re-rated, so as to refresh our portfolio. And on this point, we are really enthused about these new ideas that we continue to identify, and the upside potential that they bring to our portfolio.

New Ideas

In relation to our new ideas, we maintain a watchlist and working knowledge of a wide selection of prospective nano-cap and micro-cap companies, as well as new IPO opportunities coming to market. We continue to add to this watchlist as we meet with new companies and better understand the opportunity. When a liquidity event arises among these companies we have identified, we are able to act swiftly and with confidence, and use our relationships to access these opportunities.

To highlight the strength of the new ideas that we are reallocating our capital to, we refer back to two new positions we discussed last month.

- Corum Limited (ASX:**COO**) (purchased in September at 4.2c through sub-underwriting the shortfall of a rights issue) had a positive quarterly update, showcasing its increasing cash flows and strong balance sheet. COO finished the month at 6.2c.

- Laserbond Limited (ASX:**LBL**) (entered in September via an off-market transaction at 55c) had some positive media coverage in relation to its coating technology. There is an interesting video on this development here. LBL finished the month at 72c.

In October, we were again active in assessing a number of corporate transactions. We continue to set a high bar for the companies that we include in the portfolio, as we look for new positions that offer genuine asymmetric return potential. We participated in two placements during October. Both companies have been on our watchlist for some time - both have growing recurring revenues from Tier 1 corporate and government customers and have EVs of less than $20m.

As a side-note, we have been noticing that our increasing fund size has been advantageous for us to get preferential treatment in some nano and micro-cap placements as we can provide “institutional support and credibility” to some smaller companies shareholder registers. We often don’t have too much institutional competition in these placements as the small placement size does not really move the dial for bigger funds. We see this emerging trend as a real point of difference and source of potential excess returns for DMXCP investors.

Existing positions

As mentioned above, we are really encouraged by the new positions that we are identifying and adding to our portfolio. We are equally encouraged by the potential of our existing positions, where we note many of our longer-term positions continue to represent compelling value. We don’t know when it will happen, but, at some point, we expect the market will materially re-rate each of these positions (as was the case with EAS this month). To the extent that either the thesis has played out, or the market is obviously over-valuing the stock or the position size is no longer appropriate, we will look to sell/reduce and recycle the proceeds into fresh ideas. Some of these longer-term positions include:

- PTB Group (ASX:**PTB**), Joyce Corporation (ASX:**JYC**) and Primero (ASX:**PGX**) which are all positioned for strong growth, and are trading on less than 10x NPAT.

- Our cohort of ed-tech stocks, Kip McGrath Education Centres (ASX:**KME**), Janison Education (ASX:**JAN**) and Readytech (ASX:**RDY**) are all profitable companies, and trade on metrics far more attractive than their peers.

- Other core holdings such as AFL and SSG (both mentioned above), as well as Eureka Group (ASX:**EGH**) and Probiotec (ASX:**PBP**) had encouraging updates during the month, which support our view that they offer material upside from rather undemanding valuations.

Concluding comments

The portfolio remains very much weighted to profitable, growing, small companies on attractive valuation metrics. We continue to be disciplined and avoid unprofitable or unproven ‘story’ stocks. We have no exposure to some of the recent high profile technology focused IPOs that to us appear optimistically priced and represent a particularly frothy part of the market.

While the portfolio’s recent performance has been positive, we are acutely aware of how humbling the market can be. We remain focused, disciplined and committed to identifying the most interesting and compelling companies with low market capitalisations, in order to construct a portfolio of attractive stocks with material upside. Our cash balance is solid, and we have an increasing pipeline of interesting and prospective ideas. While we can’t control what the market does in the short term, we remain very comfortable with how the portfolio is currently positioned.

DMXCP remains open for investment from both new and existing investors. However, we note that we are presently considering our optimal fund size and anticipate letting you know shortly how we intend to slow down the inflow of funds into DMXCP. One particular constraint we have faced is that of issuing shares to new investors under the small offer provisions of the Corporations Act (which allow us to raise up to $2m from up to 20 investors in any 12 month period). We’re now very near the 20 investor limit under this provision, and appreciate the patience of any new investor relying on this provision (ie: not otherwise qualifying as a *sophisticated/wholesale investor*).

We also advise that our minimum investment for new investors has been increased to $50,000. We have the right to waive this so please let us know if this is problematic for you.

Again, for now, we remain open for investment from both new and existing investors. If you would like to discuss, Please contact Steve McCarthy on 0403 869 632 or email steven.mccarthy@dmxam.com.au

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

Kind regards



Roger Collison — *Chairman*

Steven McCarthy — *Portfolio Manager*

Chris Steptoe — *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

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	-8.42	-17.91	+8.521	+4.525	+6.213	+10.09	+8.669	+6.518	**+11.10**			**+29.66**	**-9.83**

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.