

Worth its Salt

January 2022 Update

“Doesn't it muddle up the stories?’ Haroun inquired. ‘All this turbulence must mix things up dreadfully.’ ‘No problem!’ cried Butt the Hoopoe. ‘Any story worth its salt can handle a little shaking up!’” - *Salman Rushdie, Haroun and the Sea of Stories*

Performance to Jan 31, 2021	1 month	3 months	Fiscal YTD	Last 12 months	3 years	Inception
Dragonfly Fund	-8.36%	-12.7%	+1.1%	+17.37%	+7.68% pa	+0.97% pa

Performance Hurdle: a total return greater than the five year government bond rate + 5% pa over the medium-to-long term. Fund return is calculated net of all management fees, expenses and accrued performance fees.

Fund Facts

NAV	\$1.0434
Inception	Sep 1, 2017
Bloomberg	EQUINDF AU Equity
APIR code	EQB7664AU
ISIN	AU60EQB76649

Portfolio Key Metrics

January 31, 2021	% NAV [#]
Cash (incl. cash ETF)	1%
Unlisted & Con Notes	28%
ETF	0%
Listed Equities	71%

<i>Market cap <\$100m</i>	61%

<i>Market cap \$100m-\$1b</i>	33%

<i>Market cap >\$1b</i>	5%
Top 5 positions	50%
No. positions*	32

[#] May not add up to 100% due to rounding
^{*} excludes positions <0.1%; counts multiple security types in one company as one position
 Note: In-the-money convertible notes treated as equity

Key Contributors to Monthly Performance

Best	Comms Group (CCG)
Worst	Intelligent Monitoring (IMB)

SUMMARY

- **THE MONTH** | Very few of our investments made a positive contribution to the Fund in January 2022. As the S&P/ASX Small Industrials Index fell 9.8%, Dragonfly's NAV fell 8%. It has been a tough market, with strong financial performances by some of the Fund's key holdings failing to attract investor interest and some of the more illiquid stocks like **Intelligent Monitoring (IMB)** facing weaker levels of market interest. We are investing in these companies with a view to strong medium-to-long-term returns - not trading stocks for month-to-month numbers.
- **STOCK PROFILES** | Fund investors have received profiles in recent weeks on some of those key holdings with strong financial performances, **Earlypay (EPY)** and **Medadvisor (MDR)**, via our *Small Talk* updates. We also highlighted these stocks in a recent [presentation](#) to reachmarkets.
- **REPORTING SEASON** | We are entering the peak few weeks of profit reporting for smaller companies - announcing earnings for the half-year or full-year ended December 31, 2021. Across the market there have been a few dramatic earnings downgrade events (not in any Fund holdings to-date), as there always are, but generally companies are not surprising: we track changes in analysts' consensus estimates for FY22 for micro-to-mid caps and last week the median change in revenue expectations was +0.2% while for EPS it was +0.45%, across 85 companies where there were changes.

Top Nine Positions (alphabetical order, as of January 31, 2021; ASX-listed unless otherwise stated)

Ellume (unlisted)	Energy World Corp	MedAdvisor
Energy Technologies	Geo (NZX-listed)	Scout Security
Earlypay	Intelligent Monitoring	Spacetalk

PORTFOLIO REVIEW

The portfolio was generally soft in January.

- Security monitoring company **Intelligent Monitoring (IMB)** was the poorest performed investment in the portfolio. Our interest in IMB came about when it conducted a \$32m recapitalisation in late CY2021, having previously got itself into a position where positive EBITDA was offset by too much debt. The company did \$4.3m EBITDA in FY21 and is targeting an EBITDA run-rate of >\$6m by the end of FY22 - off the ~70,000 lines it currently monitors. From there IMB's ambition is to grow that number of lines to 150,000 for \$15m annual EBITDA in 2025. IMB has a market cap of \$23m and \$21m net debt for a \$44m Enterprise Value. In its recent quarterly update, IMB stated its Board "does not believe" recent share price volatility "reflects the stability of the Business" and said it would launch a share buy-back program. IMB also said it continues to assess and progress several potential transactions that it believes would add "material value".
- The leader of the few positive contributors for the month was junior telecommunications company **Comms Group (CCG)**, where we had patiently waited for a re-rate for over a year since participating in a capital raising at \$0.08 a share in December 2020. The stock had fallen as low as \$0.065 in August 2021 and we had traded around the position through the year. While the stock closed unchanged for the month at \$0.105 a share, we sold into demand at \$0.11 a share during the month.

STATE OF THE MARKET

"Higher interest rates aren't helpful for stock prices, but the impact is different depending on the level of prices. We've already seen significant pullbacks in the major averages and even larger declines in individual stocks. Sentiment is at some of the most depressed levels we have seen in years, so we're increasingly reaching a point where a little good news could go a long way." - Bespoke Investment Group, February 2022

Equitable Investors' analysis found that >70% of micro-to-mid-caps on the ASX, ex-mining, have suffered negative returns over the past three months - and nearly half have fallen by double-digit percentages. It is easy to get lost in the noise when the market gets as volatile as it has been and inflation and interest rate worries dominate the financial media. The geopolitical activities surrounding Ukraine have only added to the unease.

We prepared the following slides for inclusion in recent presentations by Equitable Investors to put some context around the market in which we are currently operating.

State of the Market | In Summary

- We don't play the game of market prediction but seek to understand the environment we are investing in.
- The following series of charts show, among other things, that:
 - ◆ US ten year government bond rates only at levels seen just before COVID-19 impacted markets
 - ◆ The spread between bond rates and earnings yields on equities remains healthy
 - ◆ Purging of outrageously priced stocks that has caused disruption across the market
 - ◆ Volatility surged in January 2022 but remains below levels of previous periods of market disruption
 - ◆ ASX reporting season is underway and there have been less downgrades than usual
 - ◆ None of this precludes the potential for more short term volatility of course!
- Ultimately Equitable Investors believes its investors are best served by continuing to focus on investing in businesses that are priced attractively while retaining firepower to pursue new opportunities as they emerge.

State of the Market | 10 Year Government Bond Yields

Figure 1: US 10 Year Bond Yield



Figure 2: Australian 10 Year Bond Yield



Source: Marketwatch.com

State of the Market | Market-wide Equity Risk Premiums

Figure 1: S&P/ASX 300 Earnings Yield composition

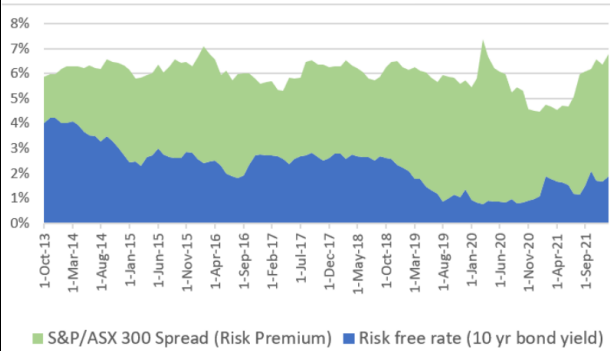
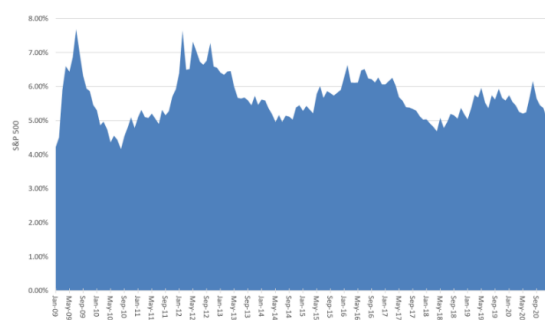


Figure 2: Implied US equity risk premium (to Jan 1, 2022)



Source: Iress, Professor Damodaran, Equitable Investors

State of the Market | Outrageous Multiples Crunched (1 of 2)

Figure 1: EV/EBITDA multiple of Netflix

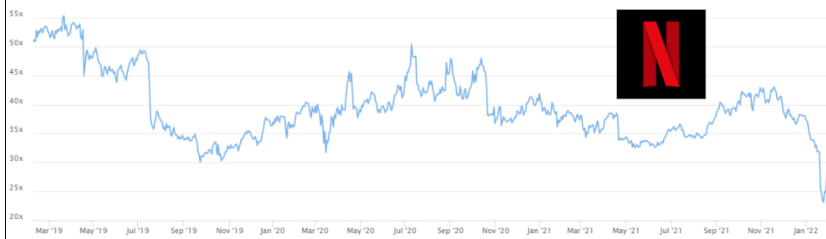


Figure 2: EV/EBITDA multiple of Zoom Video Communications



Source: TIKR

State of the Market | Outrageous Multiples Crunched (2 of 2)

Figure 3: EV/Revenue multiple of Pointsbet Holdings (PBH)



Figure 2: EV/Revenue multiple of Zip Co (Z1P)



Source: TIKR

State of the Market | Volatility

Figure 1: S&P/ASX 200 VIX



Figure 2: S&P 500 VIX



Source: Marketwatch

Fund Details

Strategy	Long only. Seeking growth or strategic value at an attractive price.
Management fee	1.5% pa
Expenses	Capped at 0.5% pa
Benchmark	5 Year Australian Government Bond Yield + 5% pa
Performance fee	20% (above benchmark)
High watermark	3 year rolling
Minimum initial investment	\$50,000, wholesale only
Investment Manager & Trustee	Equitable Investors Pty Ltd
Custodian	Sandhurst Trustees
Administrator	William Buck Managed Funds Administration (SA) Pty Ltd

Key Characteristics

Unique Opportunities	Invests in businesses that often lack widespread investor awareness.
Proprietary Research	Continually updating investment views, meeting companies, researching, evaluating.
Constructive Approach	Open dialogue with companies assists in maximising value.
Expertise	Equitable's directors have over 50 years of experience.
Alignment of Interests	Seeded by the Manager & all our best ideas go into the Fund.

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Applications to invest in Equitable Investors Dragonfly Fund can now be made online with Olivia123 - click [here](#).

**STOCK
SWAP**

Dragonfly Fund has the capability to "swap" shares in a company or companies for Fund units where Equitable Investors finds them attractive and suitable investments. To date we have used this capability sparingly, rejecting all but a very small number of proposals, but we continue to seek favourable opportunities. Further info is available [here](#).

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