Longer Horizon

February 2024 Update

"If everyone else is dashing around pricing assets on the bias of the next three months, then they are likely to misprice assets for the longer term. So an opportunity for time-arbitrage arises for the investor with a longer horizon." – GMO strategist James Montier

Performance	1 month	3m rolling	FY2024 TD	FY2023	FY2022	FY2021	Inception
to Feb 29, 2024	**+1.48%**	**+5.69%**	**+8.93%**	**-34.04%**	**-23.53%**	**+74.34%**	**-8.36%** 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	$0.56696
Inception	Sep 1, 2017
Bloomberg	EQUINDF AU Equity
APIR code	EQB7664AU
ISIN	AU60EQB76649

Portfolio Key Metrics

February 29, 2024	% NAV#
Cash (incl. cash ETF)	1%
Unlisted	9%
Con Notes in Listed	12%
ETFs	0%
Listed Equities	78%
Market cap <$100m	*93%*
Market cap $100m-$1b	*7%*
Market cap >$1b	*0%*
Top 5 positions	45%
No. positions*	26

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

Positive	De.Mem (DEM). Spectur (SP3)
Negative	Adveritas (AV1), Spacetalk (SPA)

SUMMARY

➔ **THE MONTH |** The Fund advanced 1.48% for the month as the S&P/ASX Emerging Companies Index bounced up 5% (after dropping 5.2% in January) and the median price change for micro-to-midcaps in our "FIT" universe was flat. **Spectur** (**SP3**; +22% price change) stood out among existing positions and **De.mem** (**DEM**; +19% price change) was a new, positive contributor to the portfolio.

➔ **REPORTING SEASON |** Reporting season was a reasonably orderly affair without any major surprises in the Fund's domain. We look at trends in analysts' consensus estimates as a true indicator of the strength of a reporting season. Across the market there were clearly more downgrades than upgrades across revenue, EBITDA and EPS forecasts in February. This wasn't visible in aggregate figures as the average upgrade was materially larger than the average downgrade. Size was a factor with 70%-80% of consensus revisions for sub-$250m market cap companies being negative.

➔ **SMALL TALK |** Since our last monthly update, Fund investors have received a profile of De.mem (DEM) .

➔ **OUTLOOK |** Smaller ASX listings have been out of favour for a prolonged period of time. The Emerging Companies Index is materially off its March 2022 high, as is the S&P/ASX Small Industrials relative to its August 2021 high. Trading activity among smaller listings remains subdued. We do not have a crystal ball for timing the turnaround but we do believe that this is the end of the market at which under-researched and mis-priced gems will be found.

Top Nine Positions (alphabetical order, as of February 29, 2024; ASX-listed unless otherwise stated)

Adveritas (AV1)	Intelligent Monitoring (IMB)	Spacetalk (SPA)
De.Mem (DEM)	MedAdvisor (MDR)	Spectur (SP3)
Energy Technologies (EGY)	Scout Security (SCT)	Upsure (unlisted)

PORTFOLIO REVIEW

This month we summarise some of the reporting season highlights in terms of top line growth and earnings:

Revenue Growth

- Digital ad fraud prevention tech company **Adveritas** (**AV1**; $33m market cap; -7.8% price change for the week) reported a 20% increase in 1H24 revenue as its Annualised Recurring Revenue (ARR) rose 54% year-on-year to $4.5m.
- Family safety wearables and software company **Spacetalk** (**SPA**; $10m market cap; no price change for the week) achieved 28% growth in ARR to $9.5m as 1H revenue grew 31% to $9.2m. *Disclosure: Equitable's Martin Pretty is a non-executive director of SPA*.
- Expense management platform developer **8Common** (**8CO**; $11m market cap; -11.3% price change for the week) announced a 19% increase in 1H24 revenue to $2.2m for a 37% increase in total revenue to $4.17m.

Earnings Step Changes

- Security monitoring company **Intelligent Monitoring** (**IMB**; $91m market cap; -6.3% price change for the week) reported its first set of accounts incorporating its ADT acquisition - for five of the six months of 1H24. EBITDA for the half was $14.2m of $55.7m revenue. ADT contributed $11.7m EBITDA in five months. IMB ended December 2023 with net debt of $66.9m.
- MedTech company **MedAdvisor** (**MDR**; $159m market cap; no price change for the week) booked 1H24 revenue of $75.5m, up 17.8%, lifting EBITDA 20.9% to $10.4m.
- Marine propeller and gyro stabiliser maker **Veem** (**VEE**; $178m market cap; +4.9% price change for the week) hit the higher end of first half EBITDA guidance, with $6.9m for the six months to December 31, 2023, up 65% on the prior first half. Net profit was ahead of guidance at $3.5m and up 92% year-on-year. VEE expects a similar revenue and profit outcome in the second half.
- Tradie & field services software developer **Geo** (unlisted) has entered CY2024 at EBITDA breakeven after burning $1.4m in the December half, with ARR up 23.3% year-on-year over CY2023 and both price increases and cost reductions kicking in for 2024.

Portfolio Changes

As already noted, we added water treatment company **De.mem** (**DEM**) to the portfolio during February. Investors can read our profile here. DEM conducted a $2.2m share placement in February 2024 that replenished its back account, giving it fire power to deliver on work in hand, chase new business and continue its pursuit of acquisitions - it has made four to date - to consolidate its position in the market and round out its offering. The company has been there-abouts when it comes to generating enough cash to be self-sufficient, generating positive operating cash flow in the December quarter of CY2022 and the subsequent March quarter; but burning $289k in the December quarter of CY2023. In CY2023 it grew recurring revenue to $22.5m from $19.5m in CY2022.

WHAT'S ON OUR MINDS

Liquidity in small stocks	Liquidity remains a key issue for the ASX's smaller listings. The value of trade in our proxy, the S&P/ASX Emerging Companies Index, was down 21% year-on-year in the month of February - it was the lowest dollar value of trade for February since 2019 (as was the case in January). On a twelve month rolling basis, the value of trade in the Emerging Companies Index over the 12 months to February 2024 was the lowest since the 12 months ended May 2020. We do not have statistics at hand but we expect liquidity declined to a greater degree for microcaps outside the S&P/ASX Emerging Companies Index (which has an average market cap of ~$265m).
Private Market Valuations	After highlighting a median 60% year-on-year valuation decline in US tech valuations in the June quarter, CB Insight has reported a recovery in the September quarter for some VC segments ("Series C" rounds +32% but "Series a" -4%). CB Insight noted that the valuation bump "partly a reflection of some startups not being able to raise even at low valuations as investors pursue a 'flight-to-quality' strategy". One opportunity for listed companies is to acquire or merge with unlisted businesses that can no longer hold out for high valuations. Data from ASIC, meanwhile, shows the number of Australian companies entering into external administration was up 41% for CY2023 - to a figure just over double the CY2021 level. In the first two months of CY2024 the figure is up 45% year-on-year Similarly, in the US, data from Epiq Bankruptcy showed a 72% increase in commercial "Chapter 11" filings for CY2023, relative to CY2022 - and in the month of february commercial chapter 11 bankruptcy filings climbed 118%.
"Recap" risk and opportunity	Australasian equity capital raising activity was down 23% year-on-year in the December half-year just completed and was less than half of the figure from two years earlier, using Dealogic data (in USD). We have analysed the latest round of quarterly cash flow reports (for the December quarter of 2023) and found over 230 companies with no more than four quarters of cash funding at hand based on their most recent burn rates (and backing out the R&D tax rebates many received in the quarter). Thus it continues to be the case that businesses are desperate for funding. This is a risk for existing investments that may require capital. It is also an opportunity and an exciting time for investors to apply bottom-up, fundamental research and engage constructively with companies to provide them with capital on attractive terms.
Interest rates & inflation	Interest rates remain low by historical standards and central banks should be keen to get back to something like the Taylor Rule estimate that an equilibrium policy rate is 2% above inflation. We do not see a strong case for reducing interest rates as much as the market has been forecasting in the near-term (noting the market has been becoming less bullish on rate cuts over the past month) and if central banks do walk back rates, the implication will be that the economy has deteriorated (not necessarily a great thing for businesses).
Energy	We see energy as a quasi-currency - if you have energy you hold something valuable and exchangeable. The world is going to need all forms of energy to sustain or further advance standards of living. Dragonfly Fund does not invest in the resources sector directly but we do own and seek out opportunities to participate in the energy economy - through engineering, manufacturing and software or other industrial and technological angles.
Unlisted	A key lesson for us from FY2023 is that it is important when investing in unlisted entities to have some form of influence.

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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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.