

# Change

May 2024 Update

"Change is the law of life. And those who look only to the past or present are certain to miss the future." – John F. Kennedy

Performance to may 31, 2024	1 month	3m rolling	FY2024 TD	FY2023	FY2022	FY2021	Inception
	<b>+0.01%</b>	<b>-1.70%</b>	<b>+7.07%</b>	<b>-34.04%</b>	<b>-23.53%</b>	<b>+74.34%</b>	<b>-8.29% pa</b>

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	\$0.55732
Inception	Sep 1, 2017
Bloomberg	EQUINDF AU Equity
APIR code	EQB7664AU
ISIN	AU60EQB76649

## Portfolio Key Metrics

May 31, 2024	% NAV#
Cash (incl. cash ETF)	2%
Unlisted	10%
Con Notes in Listed	10%
ETFs	0%
Listed Equities	79%
Market cap <\$100m	89%
Market cap \$100m-\$1b	11%
Market cap >\$1b	0%
Top 5 positions	44%
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	Intelligent Monitoring (IMB), MedAdvisor (MDR)
Negative	MadPaws (MPA), Spacetalk (SPA)

## SUMMARY

- **THE MONTH** | Some impressive gains by security monitoring company **Intelligent Monitoring (IMB)** and Medtech company **MedAdvisor (MDR)** would ordinarily have led to a strong month for the portfolio - but the rest of the portfolio continued the microcap struggle for investor recognition and dragged on the overall monthly return, which came in marginally positive before fees. We reduced the monthly management fee to ensure that was the case after fees as well.
- **SMALL TALK** | Since our last monthly update, Fund investors have received a [profile of MedAdvisor \(MDR\)](#) among our weekly *Small Talk* market updates for Fund investors and friends of Equitable Investors.
- **OUTLOOK** | In the short-term, the month of June is more often than not a negative month for both the Fund and the S&P/ASX Emerging Companies Index - and at the time of writing that appears to be the case once again. On the other side of that, a rebound is typically seen in July. We are also optimistic that July and August will feature financial reports from investees that demonstrate progress and value. Continuing year-on-year improvement in market activity for smaller stocks in May is noteworthy, as highlighted in *Small Talk* [here](#).
- We invest based on our view of the potential value of each individual investment. Those views evolve as we observe price, the performance of the business and changes in the operating environment. Our positive view on IMB has strengthened despite its stock price increase; whereas in "Portfolio Changes" we report that capital was reallocated from a couple of other investments - in one case cashing in on recent gains and in another cutting losses.

## Top Nine Positions (alphabetical order, as of May 31, 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

We complained in the previous report about the way the market sold down security monitoring company **Intelligent Monitoring (IMB; +30.6% price change for the month)** in April. IMB made it all back in May, with a little spare change, despite launching a capital raising for its latest acquisition. We committed to participating in this capital raising, priced at a discount to the end-of-month price, but accounted for that stock at cost price in this month's NAV.

It was the case once again in May that a great share price run for a couple of investments - on the merit of catalysts demonstrating their fundamental value - was diluted down by the general malaise of the market for small stocks.

- Last report we highlighted IMB's upgraded EBITDA guidance. This month the pro-forma FY2024 EBITDA figure is just shy of \$40m after IMB announced a \$19.3m capital raising and the acquisition of two security monitoring firms for \$15m: ACG Integration (ACG) and Alarm Assets Group (AAG). IMG said this adds \$5.7m EBITDA, taking pro-forma FY24 EBITDA to \$39.2m-\$39.7m. Last report we set out how IMB's target valuation of 10x EV/EBITDA implied 237% upside to the equity valuation. This report, post-acquisition and the share price rebound in May, that target now implies >160% upside [\$395m enterprise value less \$75m net debt; divided by 302m shares; gives you ~\$1.05 a share].
- The market had not really reacted to a strong March quarter and positive commentary from **MedAdvisor (MDR; +47% price change for the month)** but when MDR got specific with FY24 guidance, the penny started to drop. FY24 revenue will be up ~24% to between \$120m and \$123m, setting MDR up to break into profitability, with \$6.8m-\$7.6m EBITDA and \$0.5m-\$0.8m NPAT expected. That represents a ~\$12m improvement from FY23. Peloton Capital pointed out that excluding non-cash share-based payments, adjusted EBITDA is likely \$10.0m+. The simplest explanation of MDR's key revenue stream and growth engine is that it is providing big pharma with digital marketing tools that access over 218m US patients.
- No developments we were aware of explained why **MadPaws (MPA; -21% price change for the month)** was sold down during the month. Its quarterly update on April 29 showed March quarter revenue up 13% to \$6.6m and year-to-date operating cash flow of -\$0.2m over nine months, compared to -\$3.1m a year earlier. MPA said it was looking to "deliver EBITDA positive on a quarterly basis". MPA has a market cap of ~\$25m with a business growing at double-digit percentage rates; that has generated \$53m cash receipts over the past four quarters; has a market-leading position in the Australian pet care market; and burned \$1m on operating cash flow over the past four quarters, including two positive cash flow quarters among the four; with \$3.3m cash at March 31 and a marketing deal with Seven West struck in February that saw the media company taking shares (at \$0.12 a share) as payment for \$4m in advertising to be launched in FY25.
- Family safety tech company **Spacetalk (SPA; -18% price change for the month)** announced a return to Finland with that nation's leading mobile operator Elisa taking a 12-month exclusive arrangement to sell SPA's Adventurer 2 and Loop smart watches for children, with annual unit sales estimated at 5,000. SPA had reported in late April that revenue from continuing operations grew 42% year-on-year in the March quarter. Operating cash flow for that quarter was -\$1.1m as the company reiterated its target of "achieving positive free cash flow in Q4FY24". *Disclosure: Equitable's Martin Pretty is a non-executive director of SPA.*

## Portfolio Changes

MPA fell out of the Top Nine because of its price performance. During the month of May, the Fund participated in capital raisings for IMB, **Spectur (SP3; no price change for the month)** and a new position, whiskey maker **Top Shelf (TSI; -46% price change for the month)**. Funding this activity required some movement within the portfolio. We sold down our holding in **Locality Planning Energy (LPE; +38% price change for the month)** as it had moved into our valuation range and we considered there was risk that the takeover bid from River Capital did not complete, given it was not supported by the LPE board. Flow battery manufacturer **Redflow (RFX; -6% price change for the month)** was another investment we sold down.

## WHAT'S ON OUR MINDS

**Liquidity in small stocks** The last two months - April and May 2024 - have seen improved trading activity among ASX emerging companies after a long run of year-on-year declines in trading. You could say it has been a bear market in micro and nano caps since 2022. The month of April 2024, +47%, was the first month in eight that featured year-on-year growth in the value of trade across the ASX's smaller listings, using the S&P/ASX Emerging Companies Index as a proxy. The month of May was also up +13% YoY. On a twelve month rolling basis, the value of trade in the Emerging Companies Index over the 12 months to the end of May 2024 was still down 11% year-on-year - and has not been positive since August 2022.

**Private Market Valuations** We continue to watch private markets slowly adjust to reflect the change in the cost of capital that has occurred over the past two years. Clearly not all is rosy in the world of unlisted VC and PE investments. Despite marketeers labelling private assets as low volatility, there is underlying volatility in the pricing of private assets and there is correlation with public markets. The *Wall Street Journal* [reported](#) this month on how stakes in private equity funds were being traded at “big discounts to the official values set by the private-equity funds’ manager” with “buyers quickly mark[ing] up the stakes they acquire to the official value, no matter how little they paid for them”. March quarter data from PitchBook shows that “median Q1 early-stage and late-stage valuation step-ups were either flat or down” and in the secondary market shares were trading at median and average discounts of 37% and 28%, respectively. “The number of flat and down rounds as a proportion of all VC deals expanded consistently since Q1 2022 on a QoQ basis, notching 27.4% in Q1 2024—the highest level in a decade”, said PitchBook. “Common stockholders and early-stage investors face the challenge of highly dilutive terms.”

**“Recap” risk and opportunity** Australasian equity capital raising activity has improved since our last report. The dollar value raised in CY2024-to-date is up 9% year-on-year, following a 6% decline in CY2023 (using Dealogic data in USD). We analysed 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 (see 700 years of declining rates charted [here](#)) 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. Our view throughout the year has been that there was not a strong case for reducing interest rates in the near-term and that if central banks do walk back rates materially, the implication will be that the economy has deteriorated. In that context, consumer stress is becoming [evident](#) in the retail sector and savings data. Shifting market sentiment regarding the extent to which interest rates could decline from here will influence the market in the short term.

**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. Bloomberg [reported](#) this month that “electricity demands from AI data centers are outstripping the available power supply in many parts of the world” already. 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

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

## Key Characteristics

<b>Unique Opportunities</b>	Invests in businesses that often lack widespread investor awareness.
<b>Proprietary Research</b>	Continually updating investment views, meeting companies, researching, evaluating.
<b>Constructive Approach</b>	Open dialogue with companies assists in maximising value.
<b>Expertise</b>	Equitable's directors have over 50 years of experience.
<b>Alignment of Interests</b>	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](#).

Past performance is not a reliable indicator of future performance. Fund returns are quoted net of all fees, expenses and accrued performance fees. Delivery of this report to a recipient should not be relied on as a representation that there has been no change since the preparation date in the affairs or financial condition of the Fund or the Trustee; or that the information contained in this report remains accurate or complete at any time after the preparation date. Equitable Investors Pty Ltd (EI) does not guarantee or make any representation or warranty as to the accuracy or completeness of the information in this report. To the extent permitted by law, EI disclaims all liability that may otherwise arise due to any information in this report being inaccurate or information being omitted. This report does not take into account the particular investment objectives, financial situation and needs of potential investors. Before making a decision to invest in the Fund the recipient should obtain professional advice. This report does not purport to contain all the information that the recipient may require to evaluate a possible investment in the Fund. The recipient should conduct their own independent analysis of the Fund and refer to the current Information Memorandum, which is available from EI.