EQUITABLE INVESTORS®

DRAGONFLY FUND

Issued: February 2024

Do something about it

January 2024 Update

"No matter what happens, it's up to you to do something about it. Have the courage to accept responsibility, don't shy away from it, don't baulk, don't procrastinate, don't handball it to someone else.." – Neale Daniher.

Performance to Jan 31, 2024	1 month	3m rolling	FY2024 TD	FY2023	FY2022	FY2021	Inception
	-2.54%	**+6.96%**	**+7.34%**	**-34.04%**	**-23.53%**	**+74.34%**	**-8.67%** 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	$0.55869
Inception	Sep 1, 2017
Bloomberg	EQUINDF AU Equity
APIR code	EQB7664AU
ISIN	AU60EQB76649

Portfolio Key Metrics

January 31, 2024	% NAV#
Cash (incl. cash ETF)	0%
Unlisted	10%
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	47%
No. positions*	28

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	Adveritas (AV1), MedAdvisor (MDR)
Negative	Scout Security (SCT), Talius Group (TAL)

SUMMARY

➔ **THE MONTH |** Two steps forward (November and December) then one step back in January for the Fund as small stocks lost altitude. The Fund closed down 2.5% for the month as the S&P/ASX Emerging Companies Index dropped 5.2% and the micro-to-midcaps in our "FIT" universe averaged a -1.5% decline. Scout Security (SCT) and Talius Group (TAL) weighed most heavily on the portfolio.

➔ **CASH FLOW REPORTING |** Many of our portfolio companies were among those who were required to report quarterly cash flows during January. There were some very positive figures and others that have been continuing to battle on in an unfriendly environment for those not yet generating free cash flow.

➔ **OUTLOOK |** In a world where everyone seems transfixed by Nvidia more than tripling its market cap over the past year to as high as $US1.8 trillion - almost exactly matching the total market cap of the entire ASX - sub-$100m market cap companies, often with strong core shareholder bases who do not trade, are struggling for the attention of the marginal investor that sets their stock price. This in itself represents an opportunity as we look for value to be recognised in time, be it by the marginal investor or by strategic buyers looking to enhance the value of their own activities. If we were managing hundreds of millions of dollars, we see an opportunity to take anchor positions in ASX-listed micro caps and support them through to their value catalysts; to drive mergers between some; and to take others private. As we are not, we continue to roll up our sleeves and assist investees where we can to work through challenges

Top Nine Positions (alphabetical order, as of January 31, 2024; ASX-listed unless otherwise stated)

Adveritas (AV1)	MedAdvisor (MDR)	Scout Security (SCT)
Energy Technologies (EGY)	Opyl (OPL)	Spacetalk (SPA)
Intelligent Monitoring (IMB)	Redflow (RFX)	Upsure (unlisted)

PORTFOLIO REVIEW

Starting with the positive contributors for the month, digital ad fraud detection company **Adveritas** (**AV1**; market cap $38m; +14.5% share price change in the month) completed a $2.5m capital raising late in December then reported a 124% increase in December quarter cash receipts to $1.5m, burned $2m and held $3.6m cash. It said it had delivered annualised cost savings of $1.7m to be realised from the current quarter onwards. AV1 subsequently announced that in addition to its corporate customers, agencies "including multiple Fortune 500 clients)" have commenced trials of AV1's TrafficGuard.

MedTech **MedAdvisor** (**MDR**; market cap $173m; +30% share price change in the month) delivered at the top-line, reporting $75.5m revenue for the December half-year, 5% above the mid-point of its guidance, and noted a "strong pipeline for digital growth". It generated $15.2m cash from operations in the December quarter (typically its strongest quarter) for $11m over the half-year, leaving it with $22.5m cash, partly offset by $11.5m in drawn debt.

Of those stocks that dragged the most, **Scout Security** (**SCT**; market cap $2.6m; -28% share price change in the month) reported a negative $263k cash from operations in the December quarter with $58k cash in the bank. SCT said it was engaged in discussions with multiple parties in relation to additional debt funding and strategic investment and it had appointed middle market corporate advisor Westlake Securities to explore strategic opportunities in North America. Disclosure: Equitable Investors' Martin Pretty is a non-executive director of SCT.

In December we took up shares in a capital raising by an IoT player focused on aged care and health, **Talius Group** (**TAL**; market cap $21m; -18% share price change in the month). TAL rallied past the placement price in December and drifted back to the placement price at the end of January. TAL's quarterly cash flow was negative for the first time in five quarters as it invested in inventory to meet the demands of its contract with Keyton / Lendlease and other committed orders this month. TAL said it was "in the advanced stages of commercial negotiations with several potential new clients" and had "a robust pipeline comprising both confirmed orders and promising prospects, and a continuing commitment to profitability.".

Portfolio Changes

We made one notable move in January, participating in a shortfall placement for the entitlement offer conducted by **Opyl** (**OPL**; market cap $5.4m; +7% share price change in the month). This company recently appointed someone we have spent time with in the past as its interim CEO, Saurabh Jain, former CEO of Urbanise and interim CEO of Spacetalk (SPA). OPL could loosely be described as being in the biotech and drug discovery sector - but that is a sector the Fund does not play in! What OPL is doing is actually resolving the key issue we have with the space - the inability to assess the likelihood of success. OPL is a software business that built a clinical trial recruitment platform (servicing GSK among others) that struggled to get to scale - but in the background its team have leveraged AI to build a predictive tool for clinical trials, TrialKey, that claims 90% accuracy in predicting the possibility of success of any clinical trial. If you are interested, you can sign up for a free trial at trialkey.ai. We can see drug discovery companies and contract Clinical Research Organisations (CROs) leveraging this tool to improve the design of their trials and optimise the probability of success. We can also see investors in the drug discovery space using it to inform their decisions.

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 33% year-on-year in the month of January - in fact it was the lowest figure for January since 2019. For the whole of calendar 2023, the value of trade was down 24% on 2022. 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 ~$264m) - and it was less of an issue for larger companies, with the value of trade in the S&P/ASX 100 down 14% in CY2023. Lower liquidity leads to greater variability in share prices and is potentially damaging to companies' ability to raise capital.
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. Similarly, in the US, data from Epiq Bankruptcy showed a 72% increase in commercial "Chapter 11" filings for CY2023, relative to CY2022.
"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.

Applications to invest in Equitable Investors Dragonfly Fund can now be made online with Olivia123 - click here.

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.