Perennial Value Microcap Opportunities Trust

Perennial Partners

Monthly Report February 2022

	Month (%)	Quarter (%)	FYTD (%)	1 Year (%)	3 Years (% p.a.)	Since inception^ (% p.a.)	Since Inception^ Cumulative (%)
Perennial Value Microcap Opportunities Trust (Net)	-11.4	-18.5	-11.7	-13.1	14.1	18.2	133.7
S&P/ASX Small Ordinaries Accumulation Index	0.0	-7.7	-4.0	5.0	7.7	9.5	58.4
Value Added	**-11.4**	**-10.8**	**-7.7**	**-18.1**	**6.4**	**8.7**	**75.3**

^Since inception: February 2017. Past performance is not a reliable indicator of future performance.

Overview

For the month of February, the Trust was down 11.4%, underperforming the Index which was flat, as investors shunned the microcap end of the market as compared to the more liquid Small Cap Index.

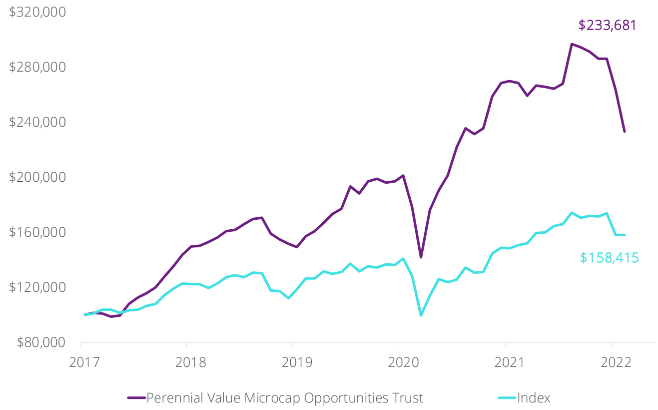
The significant weakness seen from January, reflecting expectations of rising interest rates, continued to impact stocks perceived as 'growth' but this was compounded by increased uncertainty from Russia's invasion of Ukraine, which impacted risk appetite and thus the bulk of the microcap market.

In such an environment, investors rushed for liquidity and largely ignored the fundamental news delivered in reporting season. Much of the news from companies held in the Trust were positive, particularly for some of those companies perceived as cash burners who were able to clearly show a path to positive cashflow within 12 months and had balance sheets with ample cash to achieve that.

The fact that these positive fundamentals were ignored by the market sets up the portfolio well for future returns.

The portfolio-average PE ratio of 12.9x remains at a sizeable discount to the index which is 17.1x for FY24.

Growth of $100,000 Since Inception



Performance shown net of fees with distributions reinvested. Does not take into account any taxes payable by an investor. Past performance is not a reliable indication of future performance.

Perennial Value Microcap Opportunities Trust

The aim of the Trust is to grow the value of your investment over the long term by investing in a portfolio of Australian companies that are either listed or unlisted companies found outside the S&P/ASX Top 100 Index, and to provide a total return (after fees) that exceeds the S&P/ASX Small Ordinaries Accumulation Index measured on a rolling three-year basis.

Portfolio Managers
Andrew Smith and Sam Berridge

Trust FUM
AUD $240 million

Distribution Frequency
Annual

Minimum Initial Investment
$25,000

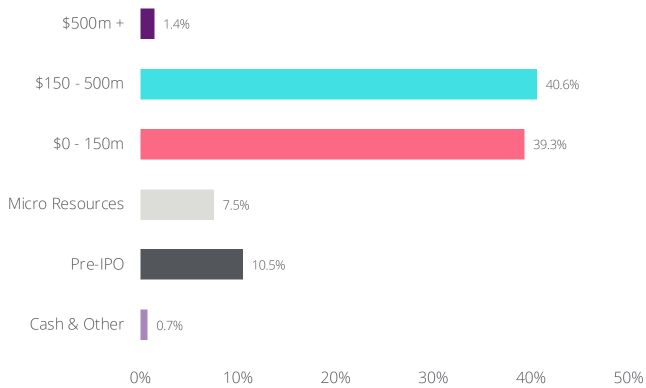
Trust Inception Date
February 2017

Fees
1.20% p.a. + Performance fee

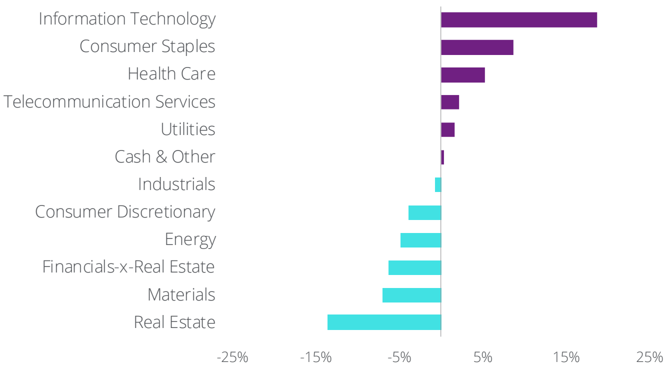
APIR Code
WPC3982AU

Top 5 Positions	Trust (%)	Index (%)
SUPERLOOP LTD	4.4	0.0
LARK DISTILLING CO. LTD	4.4	0.0
ENVIROSUITE LTD	4.3	0.0
MAGGIE BEER HOLDINGS LTD	4.3	0.0
GOOD DRINKS AUSTRALIA LTD	4.0	0.0

Market Capitalisation Exposure



Sector Active Exposure vs Index



Trust Review

The poor performance for the Trust was in stark contrast to the significant progress reported on by many of our portfolio companies during the February reporting season.

Investors in Lark Distilling (down 25.7%) were distracted given the news around the resignation of its CEO to face personal issues (extensively covered in the media). We viewed the weaker share price as an opportunity to add to what is a unique asset in the Australian market, a growing luxury brand trading below hard asset value.

We believe investors overlooked several items in this 30yr old company which had already begun a search for a new CEO back in December. The strong fundamentals were reinforced in the full result release at the end of the month:

- There is $432m of whisky inventory value at maturation using FY21 selling prices, the new information provided in the month was the expectation this value will rise by 15-25% in FY22 based on current sales trends – compared to a market cap of $253m
- 1H sales grew 78% despite the impact of COVID on many hospitability clients as well as Lark's own locations in Tasmania
- The Pontville acquisition which provides the scale needed to access export markets and high quality inventory
- Directors invested $6.4m as part of the raising for Pontville late last year

Such fundamental news being ignored, while potentially frustrating, is ultimately what enables us to acquire assets at well below our perceived true value – providing good prospects for returns going forward as growth prospects are delivered.

Other key positions where we see strong brand value and hence a strong chance of corporate interest are:

- Maggie Beer (down 0.9%) after 134% sales growth (18.2% pro-forma) and lift in EBITDA margins to 15.2%. Long time investors in the fund will recall that this position had often been a drag on performance but our patience due to the strong brand value and supporting a new CEO has been rewarded over recent months with an increased share price and investor interest
- Good Drinks Australia (down 12.3%) after delivering 15% revenue growth, fell due to investor concerns about a potential rise in WA COVID cases, their home state; we view any potential impact as transitory

Rounding out our Top 5 holdings are:

- Envirosuite (down 14.0%) which beat expectations with 14% revenue growth and 17% gross profit growth despite the drag from COVID. They finished with annual recurring revenue of $49m and $24m of cash – vs a market cap of $232m. The sales momentum also remains strong with positive tailwinds from increased ESG awareness
- Superloop (down 19.2%) with the new CEO and CFO not winning points for investor relations after a perceived cashflow miss, which after our investigation was clearly explained by the acquired Exetel working capital position. When the corrected underlying cash conversion of 97.5% was ultimately announced to the market some days later, attention had moved elsewhere. Positively, the sale of their Hong Kong and Singapore assets is due to settle in March. Sale proceeds will provide growth capital of $110m to pursue organic and inorganic growth.

One sector which has been a significant drag but remains interesting to us is Healthcare. This sector, ironically, has been one of the most impacted by COVID as regulators and customers are too distracted to consider new treatments and the often overseas based management teams are unable to meet investors (and more importantly potential customers). Thus, with borders now opening up and mobility improving, the opportunity for improved sales growth has increased and evidence of this should restore investor confidence.

Our basket of such stocks were down 36-44% for the month. Despite this, we believe the cash balance at 4DMedical (A$60m) and Lumos Diagnostics (A$15m) provide room for patience while the US economy and regulatory environment recovers from COVID. In the case of Doctor Care Anywhere, an A$11m cash raise (taking cash to A$42m) means they are now fully funded to their stated target of cashflow positive by 1HCY23. Given the market carnage, this was not picked up by the market but is very comforting to long term investors.

While the bulk of our companies are currently cashflow positive, for those that are not, we look for cash flow positivity within 18 months. In two cases, we lost conviction that the companies could achieve this and thus exited these names.

At month end, the Trust finished with 48 positions and cash of 0.7%.

Market Review – Australia (%)

S&P/ASX Small Ordinaries Index	+0.0
Energy	+8.0
Materials	+3.7
Industrials	-1.3
Consumer Discretionary	-1.7
Consumer Staples	+0.8
Health Care	-10.2
Financials	+1.2
Real Estate	+0.8
Information Technology	-11.1
Telecommunication Services	-2.8

Portfolio Managers: Sam Berridge (left) and Andrew Smith (right).

Invest Online Now

Contact us

Level 27, 88 Phillip Street
Sydney NSW 2000

1300 730 032

invest@perennial.net.au

www.perennial.net.au