LAKEHOUSE SMALL COMPANIES FUND

MONTHLY LETTER

30 September 2021

LAKEHOUSECAPITAL

Dear Lakehouse Investor,

September was another eventful month for the team as we caught the tail end of company meetings from the full year reporting season, with 24 virtual meetings across current and potential portfolio companies. We're turning over many rocks right now and, with a cash balance at 13.2% of the Fund, have plenty of dry powder with which to capitalise on further market volatility.

Fund Metrics	
Companies Held	20
Cash Allocation	13.2%
Top 5 Portfolio Holdings	33.8%
Net Asset Value per Unit (mid)	$2.2463
Fund Net Asset Value	$438.5 million
Benchmark	S&P/ASX Small Ordinaries Accumulation Index

The Fund returned -2.4% net of fees and expenses during the month compared to a -2.1% return for the benchmark. Over the last 12 months, the Fund has returned 27.2% compared to 30.4% for its benchmark. And, since inception in mid-November 2016, the Fund has produced a net total return of 189.9% compared to 73.4% for the benchmark. In annualised terms, the Fund has returned 24.4% per year since inception compared to 12.0% per year for the benchmark.

Our concentrated, growth-focused investment strategy means at times the portfolio will zig while the market zags. Our focus remains on generating long-term outperformance and the consistent execution of process, though, we are pleased with the progress made toward this goal.

	1 Month	3 Month	1 Year	3 Year (p.a.)	Inception (p.a.)
Lakehouse Small Companies Fund**	-2.4%	3.0%	27.2%	20.4%	24.4%
Benchmark*	-2.1%	3.4%	30.4%	9.4%	12.0%
Excess Return	-0.3%	-0.4%	-3.2%	11.0%	12.4%

*** Performance calculations are based on exit price with distributions reinvested, after fees and expenses, since inception in mid-November 2016. * Benchmark: S&P/ASX Small Ordinaries Accumulation Index. Past performance is not indicative of future returns.*

The Fund's largest sector allocations are to information technology (46.1% of total capital), financials (13.3%) and healthcare (9.0%) while the benchmark's largest allocations are to materials (20.5%), consumer discretionary (15.5%), and real estate (13.4%).

We embrace a bottom-up process that seeks out and emphasises businesses with extremely loyal customers, network effects, and unique and enduring intellectual property. Most of those businesses tend to end up in some specific sectors (e.g. IT) while are rarely found in others (e.g. materials), hence our continued differentiation.

Company News

Turning to specific companies, the Fund's most significant contributor to performance during the month was Altium (+19.6%) as the market responded to full year results and upgraded guidance. The biggest detractor was Pinnacle Investment Management (-8.8%) as investors reacted to the company's underlying equity market exposure during the recent bout of volatility.

The Fund's five largest holdings as of the end of the month accounted for 33.8% of the portfolio and are named in order of the Fund's allocation: Netwealth, EML Payments, Tyro, Nanosonics and Bapcor.

Altium is returning to pre-pandemic growth levels including upgrading its midpoint revenue growth forecast for the year ahead from 15.5% to 18.0%. This growth is happening alongside a continuing transition to higher levels of recurring revenue (65% of revenue in 2021) and strong growth in the number of active users of Altium 365, which allows for greater collaboration for users and long-term optionality for Altium and the customers and partners in its ecosystem. There are some short-term clouds over the business, namely a tax dispute and former-CFO making a claim over some unvested shares. We think the short-term issues will pass, as will the COVID-19 related slowdown, and we remain enthused about the business, its optionality, and a robust balance sheet with US$191 million in net cash.

Turning to Pinnacle, which has been tossed around with equity market movements. We think the market is slow to appreciate the strategic evolution in the underlying fundamentals of the business, including that it continues to broaden its earnings base away from the equities asset class. The diversification across asset classes has the added benefit -- which we observed during the COVID sell-off a little over 12 months ago -- of allowing investors to rotate out of equities and into other asset classes still within the Pinnacle stable. Pinnacle started fiscal 2022 with FUM 23% higher than the average throughout FY21, following inflows in the second half more than doubling the first half. We have seen fund-raising momentum continuing for a number of Pinnacles affiliates over recent months and we remain confident of the business' start to the new financial year.

One last thing: we mentioned Bapcor in last month's letter as the Fund's biggest detractor, but realised after publishing that we didn't expand on our thinking. Bapcor delivered strong full year results with revenue growing 20.4% and net profit 46.5%, both slightly ahead of market expectations. We were also pleased that EBITDA margins expanded across the group and that leverage is in hand with net debt relative to EBITDA sitting at just 0.74x. However, the negative impact and uncertainty of rolling lockdowns across Australia and New Zealand, particularly for Bapcor's retail-facing stores, weighed on investors' minds. Bapcor guided 'to deliver earnings at least at the level of financial year 2021, dependent on the extent of lockdowns and other government imposed restrictions', which underwhelmed investors. We remain enthused about the business and think the shares are reasonably priced at around 19 times consensus earnings estimates for this year in light of the steadiness of the business and management's history of underpromising and overdelivering. We remain patient holders.

Looking Ahead

We are continuing to turn over stones following the fresh information released with full year results. We're also seeing a pick-up in IPO and pre-IPO activity and the team are running the ruler over a number of these ASX hopefuls as potential portfolio candidates.

Thanks again to all our investors for your time and trust.

Best Regards,

Lakehouse Capital

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