

# LAKEHOUSE SMALL COMPANIES FUND

## MONTHLY LETTER

31 January 2023



Dear Lakehouse Investor,

January was a positive month for the Fund, as favourable economic data was released and some of our portfolio companies provided trading updates. The market reacted positively to the news that the Federal Reserve may be nearing the end of its interest hiking cycle. Inflation expectations continue to ease, allowing the Federal Reserve to take a less aggressive stance.

Throughout the month, we continued to deploy our cash by building stakes in our recently initiated positions and topping up on existing ideas which we believe are compelling at these price levels. Our portfolio's cash position decreased from 12.6% to 9.0%.

On to performance, the Fund returned 9.7% net of fees and expenses during the month compared to 6.6% return for the benchmark. Over the last 12 months, the Fund has returned -21.7% compared to -4.4% for its benchmark. Since inception in mid-November 2016, the Fund has produced a net total return of 86.8% compared to 53.8% for the benchmark. In annualised terms, the Fund has returned 10.6% per year since inception compared to 7.2% per year for the benchmark.

Fund Metrics	
Companies Held	22
Cash Allocation	9.0%
Top 5 Portfolio Holdings	40.9%
Net Asset Value per Unit (mid)	\$1.3018
Fund Net Asset Value	\$228.2million
Benchmark	S&P/ASX Small Ordinaries Accumulation Index

	1 Month	3 Month	1 Year	3 Year (p.a.)	5 Year (p.a.)	Inception (p.a.)
Lakehouse Small Companies Fund	9.7%	5.6%	-21.7%	-4.0%	5.0%	10.6%
Benchmark	6.6%	7.6%	-4.4%	2.4%	4.4%	7.2%
Excess Return	3.1%	-2.0%	-17.3%	-6.4%	0.6%	3.4%

*\*\* 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. Returns greater than one year are annualised.*

The Fund's largest sector allocations remain information technology (37.5% of total capital), financials (18.0%), and healthcare (16.5%) while the benchmark's largest allocations are to materials (25.2%), consumer discretionary (14.1%), and real estate (13.3%).

Our investment process seeks out and emphasises [Investment Fascinations](#); businesses with extremely loyal customers, network effects, and/or unique and enduring intellectual property. Most of those businesses tend to be more concentrated in specific sectors (e.g. technology, financials, healthcare) and rarely found in others (e.g. commodities).

We remain focused on investing in strong businesses in growing markets, with durable competitive advantages and pricing power, that are led by founders or well-aligned management teams, and with strong balance sheets.

## Company News

Turning to specific companies, the Fund's most significant contributor to performance during the month was **Pinnacle Investment Management** (+19.1%), reflecting better expectations of performance fees in the second half of the financial year. The biggest detractor was **Impedimed** (-22.8%), as the company released disappointing news with regard to its path to reimbursement. More on that later.

The Fund's five largest holdings as of the end of the month accounted for 40.9% of the portfolio and are named in order of the Fund's allocation: **Netwealth, Nanosonics, Pinnacle Investment Management, Altium** and **Promedicus**.

During the month, **Netwealth** provided a quarterly market update that was relatively weak, which is understandable considering an anaemic trading environment. Net inflows were subdued during the December quarter and were even dampened by larger than expected outflows from high net worth investors. As a result, the company lowered its net inflow expectations for FY23 to \$11 billion, from an \$11-13 billion range initially. On a positive note, the company has been able to negotiate with its banking partners higher rates on its cash balance, which will offset some of the short term weakness in inflows and higher costs. Zooming out, the company still continues to gain significant market share of net industry flows and will be in a strong position when investors start to gain confidence.

Turning to **Nanosonics**, who also provided a market update during the month. We were encouraged to see, the company has experienced a favourable pricing uptick for both capital and consumable sales in North America, largely driven by the transition to a direct sales model. The company upgraded its FY23 revenue growth and is significantly ahead of the market's expectations. We're pleased with how the company is progressing and how it has executed throughout its transition.

**Impedimed** was the portfolio's biggest detractor for the month. Investors were disappointed as the company failed to be included in the National Comprehensive Cancer Network (NCCN) Breast Cancer Panel guidelines, which means that the path to reimbursement may take a slower route. The long-term thesis for the company, however, remains on track. Core business revenue increased 38% year-over-year to \$2.2 million and the contracted revenue pipeline increased 31% year-over-year to \$18.8 million. Churn rates held steady at 2% and customer renewal rates continued to exceed 95%. Additionally, of the 34 contracts renewed in the quarter, there was a 32% increase in the average monthly licence fee, demonstrating the value of the device to existing customers. Overall, we believe that the company is making progress on its goals.

## Looking Ahead

February will be a busier month as we go through the half year results of current prospective portfolio companies. No doubt, there will be concerns around rising costs, the state of the Australian housing market, or any sign of consumer spending weakness. We will continue to deploy our cash position with an eye to owning value-generating businesses over the long run. We look forward to sharing these insights in the February investor letter.

We thank all our investors for their continued support and trust.

Best Regards,

[Lakehouse Capital](#)

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Lakehouse Small Companies Fund's Target Market Determination is available here - <https://www.lakehousecapital.com.au/lscf/>. It describes who this financial product is likely to be appropriate for (i.e. the target market), and any conditions around how the product can be distributed to investors. It also describes the events or circumstances where the Target Market Determination for this financial product may need to be reviewed.

**Disclosure:** Lakehouse, its directors, employees and affiliates, may, and likely do, hold units in the Fund and securities in entities that are the subject of this report.