

# LAKEHOUSE SMALL COMPANIES FUND

## MONTHLY LETTER

30 April 2023



Dear Lakehouse Investor,

April was a relatively quieter month for markets compared to the [events](#) of March. A number of our portfolio holdings reported their quarterly numbers, as did many of the largest businesses in the world, setting the tone for equity markets.

Turning to performance, the Fund returned 4.3% net of fees and expenses during the month compared to 2.8% return for the benchmark. Over the last 12 months the Fund has returned 1.7% compared to -9.4% for its benchmark. Since inception in mid-November 2016, the Fund has produced a net total return of 91.1% compared to 51.2% for the benchmark. In annualised terms, the Fund has returned 10.6% per year, net of fees and expenses, since inception compared to 6.6% per year for the benchmark.

Fund Metrics	
Companies Held	20
Cash Allocation	6.0%
Top 5 Portfolio Holdings	40.8%
Net Asset Value per Unit (mid)	\$1.3318
Fund Net Asset Value	\$223.2 million
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*	4.3%	2.3%	1.7%	0.7%	6.5%	10.6%
Benchmark**	2.8%	-1.7%	-9.4%	9.2%	3.9%	6.6%
Excess Return	1.5%	4.0%	11.1%	-8.5%	2.6%	4.0%

\* Performance calculations are based on exit price with distributions reinvested, after fees and expenses, since inception in mid-November 2016. Returns greater than one year are annualised. Past performance is not indicative of future returns

\*\* Benchmark: S&P/ASX Small Ordinaries Accumulation Index.

The Fund's largest sector allocations remain information technology (35.6% of total capital), financials (20.8%) and healthcare (20.1%), and while the benchmark's largest allocations are to materials (26.7%), consumer discretionary (16.5%), and real estate (12.9%).

As we remind investors each month, 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).

## Company News

Turning to specific companies, the Fund's most significant contributor to performance during the month was **Impedimed** (+76.2%) following a transformative development for the company. The biggest detractor was **Frontier Digital Ventures** (-28.1%), as the company raised capital at a deep discount to the prevailing share price. More on both companies shortly.

The Fund's five largest holdings as of the end of the month accounted for 40.8% of the portfolio and are named in order of the Fund's allocation: **Nanosonics**, **Netwealth**, **Altium**, **Xero** and **Pinnacle Investment Management**.

Moving to our biggest contributor, medical device company Impedimed, which is a smaller holding in the portfolio and one we discussed in the [January 2023 letter](#) when it was the Fund's biggest detractor. The share price jumped in late March, and continued in April, as the National Comprehensive Cancer Network (NCCN) released updated guidelines that accelerate Impedimed's path to insurance reimbursement for its core product, Sozo, which helps identify and monitor lymphedema in breast cancer survivors.

There were two particularly notable components to the updated guidelines. Firstly, it was a Category 2A recommendation, meaning there were no votes against by the 28 member panel. This should smooth the path to reimbursement as most large private insurance companies use the Category 2A recommendations as the basis for coverage policy determinations. This view was strongly validated in the first three weeks following the updated guidelines as two thirds of the target insurance payors provided notification to Impedimed of their intention to review – primarily out of cycle reviews – to consider Sozo reimbursement.

Secondly, the updated Guidelines recommend regular screening for lymphedema, including with bioimpedance spectroscopy (BIS), for *all* patients at risk of limb lymphedema (not just breast cancer survivors), materially expanding Impedimed's addressable market. The company has a big execution lift in the months ahead to take advantage of this leap forward for the business and their first-mover position as the only FDA-cleared BIS technology for the assessment of lymphedema. Both prices and volumes should accelerate materially as payors adopt the updated guidelines and add Sozo to their reimbursement list, with potential for Sozo to expand its addressable market into other areas of oncology.

Finally, we should touch on the performance of the underlying business, before the impact of updated NCCN guidelines. Annual recurring revenue grew 28% to \$9.8 million in the quarter, and churn remains very healthy at less than 2%. Reimbursement adoption will rapidly accelerate revenue growth, though we are mindful the company is still burning cash at around \$3 million per quarter, has \$26 million in funds

available, and needs to invest further to take advantage of their favourable market position. We are optimistic about the company's future and supportive of an acceleration in investment to drive growth.

The biggest detractor for the month was another smaller holding, Frontier Digital Ventures, which raised capital early in April at a 19.4% discount to the prior close, and the share price subsequently followed. A raise to fund A\$26.1 million in earnout payments was widely anticipated, and well supported by institutions, resulting in it being upsized from \$10 million to \$13 million.

The business has faced a mixed operating environment for its portfolio of online classifieds businesses across emerging markets, to which the board responded with strong cost controls. Despite revenue falling 10% to \$18.2 million in the quarter, operating margins actually expanded three percentage points to 11% through the focus on costs. The slowdown at the portfolio-level was mostly attributed to Zameen's softer performance, driven by weak economic conditions in Pakistan and the material weakening of its currency compared to the Australian Dollar, however this didn't stop the business from generating \$2.0 million in operating earnings for the quarter.

Netwealth also provided an update during April, albeit a weaker-than-expected quarter with funds under administration (FUA) growing at an annualised 14.3%. The reduced pace of the business led management to trim full year guidance, implying full year growth in the mid-teens instead of the previously slated low-twenties. We remain comfortable with this growth given the current market distractions, inherent operating leverage in the company, and widening margins as the business rolls past a heavy investment phase ahead of launching additional platform features.

SiteMinder reported good quarterly figures, with revenue and annualised recurring revenue (ARR) up 28.7% and 28.5%, respectively. The travel recovery in Asia remains robust, led by the resumption of outbound travel from China. This has led to an acceleration of net subscriber additions and a surge in forward bookings, which sets the company up for a strong fourth quarter performance. The company continues to work on its path to profitability, improving underlying free cash outflow margins by 5.5 percentage points compared to the first half of fiscal 2023. Management have reiterated that the company will reach breakeven by the final quarter of fiscal 2024, as the recent cost out program sees its full impact. Overall, we are pleased with the company's performance and expect further improvements on the profitability end.

## Looking Ahead

As we work through May, confession season is upon us with companies providing any final changes to full year guidance – and confessions – ahead of the 30 June close. The portfolio hasn't suffered any major surprises at the time of writing, and we look forward to updating our investors of material new information in due course.

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

Best Regards,

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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.

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