

LAKEHOUSE SMALL COMPANIES FUND

MONTHLY LETTER

31 July 2023



Dear Lakehouse Investor,

Most ASX companies were bunkered down in July compiling their financial year accounts. Some of the Fund's holdings released quarterly cash flow reports providing valuable updates and insights to their full year results.

As we progress further into 2023 the macroeconomic environment continues to improve, with inflation moderating and 10-year bond yields stabilising. Against this backdrop, investors have begun to shift their focus back to fundamentals which, broadly speaking, has been a net positive for the type of long-duration, high-quality growth companies that Lakehouse typically focuses on.

Fund Metrics	
Companies Held	21
Cash Allocation	7.1%
Top 5 Portfolio Holdings	37.0%
Net Asset Value per Unit (mid)	\$1.4298
Fund Net Asset Value	\$232.2 million
Benchmark	S&P/ASX Small Ordinaries Accumulation Index

The Fund returned 6.0% net of fees and expenses during the month compared to 3.5% return for the benchmark. Since inception in mid-November 2016, the Fund has produced a net total return of 105.2% compared to 51.5% for the benchmark. In annualised terms, the Fund has returned 11.3% per year, net of fees and expenses, since inception compared to 6.4% per year for the benchmark.

	1 Month	3 Month	1 Year	3 Year (p.a.)	5 Year (p.a.)	Inception (p.a.)
Lakehouse Small Companies Fund*	6.0%	7.4%	14.5%	-1.8%	5.9%	11.3%
Benchmark**	3.5%	0.2%	0.8%	5.9%	3.2%	6.4%
Excess Return	2.5%	7.2%	13.7%	-7.7%	2.7%	4.9%

* 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 as of the end of July were to information technology (35.5%), financials (19.6%) and healthcare (18.6%), while the benchmark's largest allocations are to materials (24.5%), consumer discretionary (16.7%), and real estate (12.9%). We expect to have material allocations to these sectors over time as the sectors, or at least subsets of them, are overweight business models that lend themselves to strong long-term performance, namely intellectual property, network effects, and loyalty.

Company News

Turning to specific companies, the Fund's most significant contributor to performance during the month was **SiteMinder** (+44.2%) on the back of a solid quarterly update and a stronger focus on profitable growth going forward. More on that shortly. The biggest detractor was **Objective** (-4.0%), which underperformed on no material news.

The Fund's five largest holdings as of the end of the month accounted for 37.0% of the portfolio and are named in order of the Fund's allocation: **Netwealth**, **Nanosonics**, **Pinnacle Investment Management**, **Xero** and SiteMinder.

SiteMinder delivered a strong quarterly update and grew into the Fund's top 5 positions. The company reported revenue and annualised recurring revenue (ARR) growth of 27.3% and 24.1% (in constant currency), respectively. The overall travel industry continues to post strong growth, despite concerns around slowing consumer spending. SiteMinder's pipeline remains healthy, ending the quarter with 39,100 property subscribers, up 12.7% year-on-year. Property subscribers added during the half accelerated to 2,500 compared to 1,600 in the previous half and 1,300 in the same period in the prior year. Aside from subscriber (volume) growth, recent pricing and product related initiatives will continue to support growth in future years.

As discussed in our [recent annual letter](#), the business is at a fundamental inflection point as it closes in on cash flow breakeven. Management has incrementally brought forward guidance, and now expects to be free cash flow positive for the entirety of the second half of fiscal 2024. This recent quarter revealed a more than 10 percentage point sequential improvement in underlying free cash flow margins, which is impressive considering the acceleration in key business metrics. We believe the company will gain a wider investor audience as it crosses into profitability and its attractive economics become more visible.

Turning to Netwealth, which provided its final quarterly update during the month. The wealth platform has experienced a period of elevated outflows as investors have sought to pay down (increasingly expensive) debt and/or pursue higher off-platform interest rates. Despite this challenging macroeconomic backdrop, and tepid advisor appetite to change platforms, the business grew funds under administration 26% in fiscal 2023 to \$70.3 billion. The platform is now approaching 7.5% market share, compared to a third of that four years ago, and stands to benefit from increasing scale and widening margins following a period of investment in the years ahead. We look forward to a comprehensive update on the business when it reports full year results on 16 August.

Pinnacle also provided a market update during July and, in typical form, quickly followed up with its full year results in early August. Net profit was in line with last year, and consensus expectations, at \$76.5 million. The business faced a tough fundraising environment throughout fiscal 2023, but there are signs that this may be thawing with a big turnaround in net inflows in the second half of \$3.0 billion, compared to \$1.5bn of net outflows in the first six months.

The business remains well capitalised with \$67.2 million in net cash, plus \$100 million in additional liquidity, leaving it well placed to continue investing for longer-term growth. A total of around \$28 million was invested in growing existing affiliates during the year, half of which was funded by Pinnacle. We are big fans of this growth avenue given the strong alignment and significant operating leverage, and returns, on offer. Heavier investment in these areas bode well for when the market turns and the longer term growth of Pinnacle's proven business model.

Looking Ahead

With the full year reporting season upon us, we are looking forward to hearing more from the management teams of the Fund's portfolio holdings, prospective companies, and their plans for the future.

As always, 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.

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