



Spheria Emerging Companies Limited (Company)
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19 July 2024

By Electronic Lodgement

Market Announcements Office
ASX Limited
20 Bridge Street
Sydney NSW 2000

Dear Sir/Madam

Spheria Emerging Companies Limited (ASX:SEC) – Monthly Investment Update

Please find attached a copy of the investment update for the month ending 30 June 2024.

For further information, please contact 1300 010 311.

Authorised by:

Calvin Kwok
Company Secretary

Overall Commentary

The Company returned -0.9% (after fees) during the month of June, outperforming the S&P/ASX Small Ordinaries Accumulation Index by 0.5%.

Company Facts

Investment Manager	Spheria Asset Management Pty Limited
ASX Code	SEC
Share Price	\$2.220
Inception Date	30 November 2017
Listing Date	5 December 2017
Benchmark	S&P/ASX Small Ordinaries Accumulation Index
Dividends Paid	Quarterly
Management Fee	1.00% (plus GST) per annum ¹
Performance Fee	20% (plus GST) of the Portfolio's outperformance ²
Market Capitalisation	\$132.7m

¹ Calculated daily and paid at the end of each month in arrears.

² Against the Benchmark over each 6-month period to a high-water mark mechanism

Performance as at 30 June 2024

	1 Month	3 Months	1 Year	3 Years p.a.	5 Years p.a.	Inception p.a. ³
Company ¹	-0.9%	-7.1%	6.9%	0.1%	6.3%	6.2%
Benchmark ²	-1.4%	-4.5%	9.3%	-1.5%	3.7%	4.3%
Difference	0.5%	-2.6%	-2.4%	1.7%	2.6%	1.8%

¹ Calculated as the Company's investment portfolio performance after fees excluding tax on realised and unrealised gains/losses and other earnings and after company expenses

² Benchmark is the S&P/ASX Small Ordinaries Accumulation Index.

³ Inception date is 30 November 2017. Past performance is not a reliable indicator of future performance. All p.a returns are annualised.

Net Tangible Assets (NTA)¹

Pre-Tax NTA²

2.231

Post-Tax NTA³

2.239

¹ NTA calculations exclude Deferred Tax Assets relating to capitalised issue related balance and income tax losses. These figures are subject to audit.

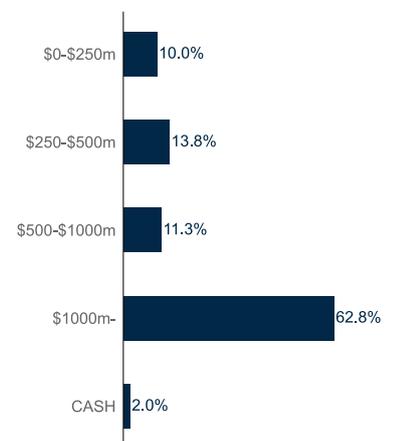
² Pre-tax NTA includes tax on realised gains/losses and other earnings, but excludes any provisions for tax on unrealised gains/losses.

³ Post-tax NTA includes tax on realised and unrealised gains/losses and other earnings.

Top 10 Holdings

Company Name	% Portfolio
Bega Cheese Limited	5.1
Healius Limited	4.9
Supply Network Limited	4.3
IRESS Limited	4.1
The Star Entertainment Group Limited	3.3
Deterra Royalties Limited	3.2
Breville Group Limited	2.9
GWA Group Limited	2.9
Magellan Financial Group Limited	2.8
Fletcher Building Limited	2.7
Top 10	36.1

Market Cap Bands



Source: Spheria Asset Management

Markets

Smaller companies continued to drift lower over June with micro caps and smaller companies under performing large caps. While trying not to turn ourselves into macro economists it was pertinent to note that Canada, the ECB (Eurozone), Switzerland and Sweden all cut interest rates over June by 25bps. Several major countries – the US, UK and Australia all held rates over the month with the US providing its strongest hints yet that rates could come down later in the year. This is relevant because our view is that the Australian economy is rapidly moving into a recession like situation which has been somewhat masked by high immigration and the drawdown of significant personal savings consumers built up during the Covid period. With these buffers now showing signs of exhaustion, we are starting to see companies struggle to grow topline and maintain cost discipline.

Cost reduction hasn't been a strong skill set amongst Australian corporates and to be fair, hasn't for some time been a core skill requirement. Given a tougher consumer outlook with some wage pressures still evident, now is the time to flex these muscles. Cost reduction, innovation and staff motivation will be key differentiators between how smaller companies execute over the next 12-18 months.

Major Contributors to Performance

Over the month the largest contributors to performance were from overweight positions in Healius (HLS.ASX, +18%), Star Entertainment Group (SGR.ASX, +9%) and Regis Healthcare (REG.ASX, +10%).

Healius (HLS.ASX) share price rose 18% during the month after the company provided a trading update for the 2024 financial year which implied a significant second half improvement in operating performance, with the business expecting to generate \$60-65m underlying EBIT for the full year to 30 June 2024. Improving pathology volumes, a moderating rate of inflation, and a much-needed focus on costs and productivity provide the foundation for continued margin improvement off the 1H24 lows. The imaging business is currently up for sale with interest from multiple parties driving some welcome competitive tension into the process. The sale proceeds will be more than sufficient to leave Healius with a net cash balance sheet. As the 2nd largest player in a consolidated Australian pathology market (top 3 comprise ~70%) we continue to be attracted to the business over the long term and see further material upside to the current share price.

Major Detractors from Performance

The largest detractors from performance included overweight positions in City Chic Collective (CCX.ASX, -51%), Deterra Royalties (DRR.ASX, -14%), Skycity Entertainment Group (SKC.ASX, -16%).

City Chic Collective (CCX.ASX) share price fell over 50% in June after the company announced a capital raise and trading update for the financial year. Trading conditions have remained challenging with sales expected to be down 30% for the 2024 financial year as higher interest rates have significantly impacted consumer spending for CCX's core demographic. As a result, the business has undergone a strategic review to simplify the business and realign the cost base (expecting to strip out \$20.3m of cost). The capital raise of \$23m (\$17.5m underwritten), offered at a 50% discount to the last closing price, will be used to support the balance sheet and re-structure the business after the sale of the UK and US businesses. Post the raise the business will have ~\$10m of cash and a \$10m debt facility available. The recent trading update was disappointing as we had expected trading conditions in the business to have stabilised. With the business now greatly simplified back to the Australian core and a stronger balance sheet we believe the business can cycle through the tough economic environment.

Outlook & Strategy Going Forward

As we discussed last month, Australia is lurching toward recession like conditions. Backward-looking statistics aren't fully reflecting the toughening labour market conditions nor capturing consumer sentiment. Merely raising prices (as cafés around us want to do) without looking to trim costs where possible is going to see consumers shift their preferences. We are entering a time when better management teams will earn their stripes. We think the upcoming reporting season could be a tough one for smaller companies, however this is likely to somewhat assist Central Banker's moves with respect to interest rates which in turn will go some way to stimulating the recovery in the economy. We believe businesses with strong balance sheets and a proven ability to generate cash are likely to come through market challenges in better shape and we continue to focus on unearthing these types of opportunities.

Fund Ratings



Contact Us

For more information, please contact Pinnacle Investment Management Limited on 1300 010 311 or email distribution@pinnacleinvestment.com

Disclaimer

Spheria Emerging Companies Limited (the Company, ASX: SEC) is a listed investment company (LIC) that provides investors with access to an actively managed, Australian and New Zealand small and micro companies portfolio, designed for investors seeking capital growth and portfolio diversification. It is a confined capacity investment strategy that identifies smaller companies where the present value of cash flows can be reasonably determined and they are assessed to be trading at a discount to their intrinsic value. The smaller companies universe is more volatile and higher risk. An experienced investment manager in the small company end of the market is paramount to success, for this reason there are only a small number of listed investment companies offering access to a diversified small companies investment portfolio. Spheria Asset Management Pty Ltd (the Manager, Spheria), is the appointed investment manager and is a specialist team with a track record of navigating the higher risk opportunities at the small end of the market.

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