

Spheria Global Opportunities Fund

ARSN 627 330 287 APIR WHT6704AU

Performance as at 31st October 2022

	1 Month	3 Months	1 Year	3 Years % p.a.	Inception p.a ³
Fund ¹	8.3%	0.2%	-16.3%	10.6%	10.9%
Benchmark ²	8.5%	1.9%	-9.6%	5.5%	5.6%
Difference	-0.2%	-1.7%	-6.7%	5.2%	5.3%

¹ Spheria Global Opportunities Fund. Returns of the Fund are net of applicable fees, costs and taxes.

² Benchmark is MSCI World Small Cap Index (net in AUD) for all periods. Please note that the Benchmark from inception to 30 June 2021 was the MSCI Kokusai Microcap Index (net in AUD) and from 1 July 2021 to 30 September 2022 was the MSCI World Microcap Index (net in AUD).

³ Inception date is 1 March 2019. Past performance is not a reliable indicator of future performance. All p.a. returns are annualised.

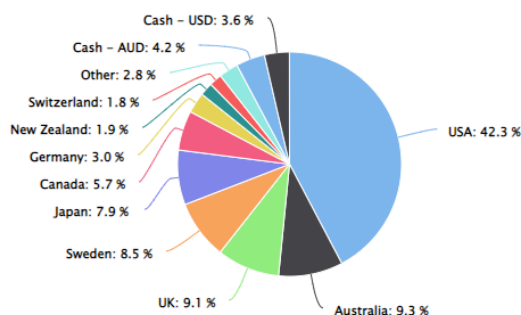


Overall Commentary

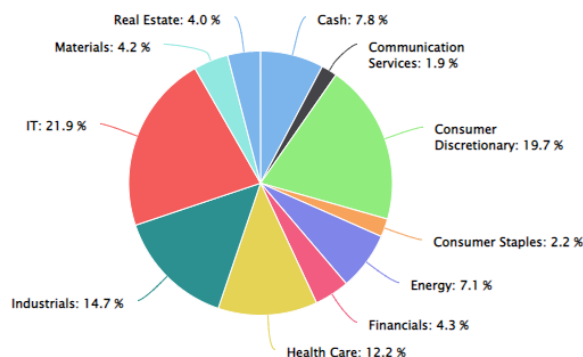
The Spheria Global Opportunities Fund increased 8.3% (after fees) in AUD terms during the month of October, underperforming the MSCI World Small Cap Index by 0.2%. In USD terms, the MSCI World Small Cap index increased 8.1% after the USD gave back some of its recent gains.

Regional Exposure

Sector Exposure



Source: Spheria Asset Management



Markets

Markets rebounded strongly in October driven by a combination of "the technicals" (always easier to identify in hindsight) and nascent hope that inflation may be peaking.

The rally was led by cyclicals in the energy, financials, industrials, and consumer discretionary sectors, which outperformed the lower beta healthcare, utilities and real estate sectors. Asian markets lagged the US and Europe as China's zero-Covid policy continued to weigh on the region, whilst declines in the Yen offset Japanese gains in local currency.

Bond yields were relatively flat over the month and yield curves remained inverted, signaling that weaker macroeconomic conditions likely loom in the months ahead.

But as we've noted in previous reports, markets have had ample time to digest and price many of these risks. The recent shift in sentiment is a recognition of the fact that, for the time being at least, the balance of these risks lies to the upside.

We have also been pleased to observe recent performance being driven in large part by 'real companies' with real cash flows. A continuation of these trends post month end reinforces our confidence that, after an extended hiatus, rewards for skillful fundamental investing are on offer here and now.

With that in mind, and a degree of conservatism in our forecasts, we continue to look for the best opportunities across the market as we rotate into companies that we previously felt were too expensive and / or had material and underappreciated earnings risks.

Major Contributors for the Month

Core Laboratories (CLB.US) – increased 45% in October on a stronger oil price signaling that CLB's services will be required for some time to come. CLB provides reservoir description and production enhancement services to the oil and gas industry. The company helps oil companies across the globe determine how much oil or gas is present in their reservoirs and how quickly it can be extracted. The company's operating results are improving, with Q3 revenue and earnings surpassing market expectations, albeit off a depressed base. The backdrop is still one of capital discipline for CLB's customers, with the availability of frack crews and drilling rigs also constraining growth. The company wisely continues to prioritize debt repayment and whilst it trades on elevated multiples, earnings are depressed and we continue to believe the probabilities are positively skewed at the current share price.

Weis Markets Inc (WMK.US) – Increased 32% in the month, as investors re-rated this Mid-Atlantic focused US grocery retailer on minimal news-flow. Weis's Q3 result was released on the final day of the month, revealing a solid, if not exceptional set of financials. Sales are growing but earnings are pretty flat as the company wrestles with the same inflationary pressures being faced the world over. We remain attracted to WMK's defensive attributes, net cash balance sheet, and reasonable valuation at 13.5x this year's EBIT.

Nitro Software (NTO.AU) – increased 29% over the month after receiving an improved takeover bid from local private equity investor and 20% shareholder Potentia at A\$1.80, surpassing its previously rejected A\$1.58 bid. Potentia's improved bid was promptly bested by a A\$2.00 cash offer from KKR-backed Canadian software company Alludo. Nitro provides PDF editing software to enterprise customers across the globe helping them to improve document productivity, as well as eSigning software that offers high-trust digital signature solutions in a market where security and compliance is increasingly in focus. Revenue is growing strongly (+36% in 1H22), led by high value subscription revenue which now comprises 72% of the total. The business is currently loss-making, but management expects to be cash flow positive from 2H23. Our fundamental valuation remains well above the latest bid, and we remain hopeful that this gap is bridged.

Major Detractors for the Month

Inogen Inc (INGN.US) – declined 14% in October. Inogen manufactures portable oxygen concentrators (POC) for patients that require long-term oxygen therapy, typically those with COPD (chronic obstructive pulmonary disease). POCs can replace bulky oxygen tanks and cylinders which are not portable and require periodic refilling. The company operates a direct-to-consumer model as well as B2B. The business is modestly growing revenue as it recovers slowly from Covid-related disruption, whilst input cost and wider inflationary pressures mean the company will remain loss-making for some time yet. Its cash balance is diminishing but remains relatively high at US\$185m, affording Inogen at least a few years to achieve positive cash flow. We recently exited this position and redeployed into companies that we believe offer better a risk reward tradeoff.

MCJ Co Ltd (6670.JPN) – declined 7% in October, underperforming both global and local indices over the period. MCJ is a PC and peripheral retailer with a focus on high-end custom-built PCs. It has a long operating history and is the biggest Japanese domestic PC retailer with approximately 80 stores. The business is exposed to the rapid growth in e-sports and deregulation of competitive gaming in Japan. During the month MCJ upgraded guidance for the half year to 31 March 2023, raising expectations for revenue and EBIT by 3% and 8% respectively. Despite this, growth is plateauing as Covid-tailwinds subside, with the stock's recent underperformance likely an acknowledgement of this pattern. At a forward EBIT multiple of 6x and 14b Yen of cash on its balance sheet, MCJ continues to have valuation support.

Alcoa Corp (AA.US) – declined 7% in October after generating an operating loss in Q3 due primarily to a 22% qoq revenue decline resulting from falls in the alumina and aluminium prices. Higher input costs are also hurting its high-cost European plants, where Alcoa is sensibly curtailing production. Further losses in FY23 are possible, if not likely, given the backdrop of softening demand and a high fixed cost base. Near term upside could come from a ban by the US on Russian aluminium imports (6% of global production), which the authorities are currently considering. Further, a significant proportion of the world's alumina and aluminium production is cash negative, which should drive further curtailments across the industry and provide medium term support to pricing. Longer-term demand is underpinned by EV and light-weighting across all vehicle types, as well as the use of aluminium in the development of renewables infrastructure. Alcoa has a market cap of \$8.7b, modest net debt, and should earn US\$1b of EBIT in a normal market, more than justifying the current share price in our view.

Outlook & Strategy

We are not expert macroeconomic forecasters. Instead, we focus our combined efforts on bottom-up stock selection, favouring companies with wide economic moats, strong balance sheets, the ability to generate strong cash flows, and fundamental valuation support. This puts investors in the best position to achieve superior risk adjusted returns over the long run.

We see our approach as little more than placing a series of high probability bets, constituted into a portfolio with a variety of economic exposures. We will not get everything right. But by being disciplined and 'playing the odds', we are giving investors every chance to outperform.

Buying loss-making businesses on 10x revenue is the antithesis of what we do. That's not to say that such an approach cannot be successful, for a time at least (as the last several years have shown). It's just not a high probability way to invest, in our view.

As is always the case, the outlook is clouded. Political tensions remain high, and the economic backdrop appears certain to remain volatile. Volatility can make people uncomfortable as it's often disorienting. Discomfort and disorientation are unhelpful qualities for investing. Adherence to a dependable process during times like these should allow us to profit from the discomfort of others.

With the market increasingly discriminating between companies that offer fundamental value versus those that offer hope and a nice story, we are investing with the winds at our tails for the first time in a long time.

Platform Availability List

The Spheria Global Opportunities Fund is available on the below Platforms. Please check with your platform for minimum investment requirements and fees.

BT Panorama

HUB24

Macquarie Wrap

Netwealth

Praemium

Spheria Global Opportunities Fund	
Benchmark	MSCI World Small Cap Index
Investment Objective	Outperform the MSCI World Small Cap Index in AUD (Net) over the long term
Investing Universe	Global listed small cap and microcap companies with a market capitalisation equal to or lower than the market capitalisation of the largest issuer in the MSCI Global Small Cap Index at the time of purchase
Holdings	Generally 30-80 stocks
Distributions	Annually
Fees	1.10% p.a. management fee & 20% performance fee of the Fund's excess return versus its benchmark, net of the management fee
Cash	Up to 20% cash
Expected Turnover	20% - 40%
Style	Long only
APIR	WHT6704AU
Minimum Initial Investment	\$25,000

Fund Ratings



Further Information

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

Disclaimer

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Link to the [Product Disclosure Statement](#)

Link to the [Target Market Determination](#)

For historic TMD's please contact Pinnacle client service Phone 1300 010 311 or Email service@pinnacleinvestment.com

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