# Renaissance Emerging Companies Fund
# Quarterly Report – March 2024

Renaissance Asset Management

## Fund Performance

| | 3 Months | 1 Year | 3 Years p.a. | 5 Years p.a. | 10 years p.a. | Since Incept. p.a.^ |
|---|---|---|---|---|---|---|
| **Renaissance Emerging Companies Fund*** | 4.17% | 14.76% | 3.54% | 15.39% | 16.82% | 14.08% |
| **S&P/ASX Small Ords Acc. Index** | 7.55% | 13.83% | 2.72% | 5.43% | 6.56% | 5.78% |
| **Value added** | -3.38% | 0.93% | 0.82% | 9.97% | 10.26% | 8.30% |

*Fund returns are calculated net of all fees and expenses and assume reinvestment of distributions. Past performance is not a reliable indicator of future performance, the value of investments can go up and down. The fund name was changed from Renaissance Smaller Companies Fund to Renaissance Emerging Companies Fund as of 1 July 2015. The Information Memorandum was changed to reflect name and change of strategy for this fund from a small cap strategy to an emerging company's strategy. Please refer to the Information Memorandum for further details. ^ Inception date 1 July 2004.

## Portfolio Commentary

For the March quarter, your portfolio returned 4.2% whilst the Small Ordinaries benchmark returned 7.6%, resulting in underperformance of 3.4%. For the year to March, the Portfolio returned 14.8% while the benchmark returned 13.8%, outperforming by 0.9%.

### Index Returns

| Index | Qtr % | 1 Year % |
|---|---|---|
| **Small Ords** | 7.5 | 13.8 |
| **Small Industrials** | 9.6 | 20.5 |
| **Small Resources** | 1.4 | -2.8 |
| | | |
| **ASX 100** | 5.2 | 14.5 |
| **ASX 100 Ind.** | 9.6 | 20.1 |
| **ASX 100 Res.** | -6.4 | 0.2 |

### *Your Portfolio*

Australian markets produced solid gains over the period with the S&P ASX 100 up 5.2% and the S&P ASX Small Ords returning 7.6%. The Australian economy grew by 0.2% q-o-q to end of 2023, which although in line with forecasts was still soft by Australian standards. Inflation remained steady over the quarter with the RBA remaining tight lipped with regards to providing forward guidance, although they do suggest the next move in rates will be down, the RBA seems to be in no hurry and is happy to wait until inflation reaches their target range.

The Small Ordinaries Index returns were driven by larger Index stocks including Life 360 (+73%), Paladin Energy (+39%), CSR (+34%), Megaport (+63%), ZIP Co (+119%) & Telix (+28%) and micro-cap stocks lagged the broader small-cap market. Your portfolio shared in the gains with some good stock selection in Veem Ltd (+62%), Austin Engineering (+49%), Genetic Signatures (+56%), Amaero Int (+62%), Prophecy Int (+33%) and Aurelia Metals (+41%). Regardless, we are disappointed by the return which fell short of the benchmark, and we have reviewed some investments that were not delivering. Whilst we see valuation support for some of these investments, where headwinds have emerged, we have sold to reinvest in new ideas. To that end we sold out of the following: Redflow Ltd, Kip McGrath Education, Swoop Holdings, Birddog Technology & Wagner Holdings (this performed well but we didn't build a big enough position at better prices). We took profits in the following: Austin Engineering, Motorcycle Holdings, Acrow Ltd, IPD Group, Veem Ltd and Aurelia Metals. We did add some new investments during the quarter including Trajan Group, Adacel Technologies, Wagner Holdings, Pioneer Credit and Calidus Resources.

The key stocks that added value to your portfolio during the quarter included Veem Limited, Austin Engineering, Genetic Signatures, Amaero Int and Prophecy International. The key stocks that detracted value from your portfolio included Close the Loop, Fleetwood Ltd, Antipa Minerals, Big River Ltd and Synertec. We will continue to review these positions.

***Trajan Group (TRJ) – has it been through the worst, we think so…***


TRJ was a successful new listing in 2021 and offered exposure to a founder led business in the life-sciences industry which had growth, operating earnings, and cash flow as well as numerous growth options. The market liked the stock as they were leveraged to new equipment sales but also consumables and the business had a strong moat. TRJ also demonstrated growth through acquisitions and management seemed capable of extracting synergies (sales & costs) whilst growing a global footprint. The stock performed well, and it attracted a hefty multiple when it was trading in the $4-$4.50 range. The company missed on some results, and it started to underperform, and we took a good look last year, but the first half results provided an entry point as the share price traded around $1.10 or about 75% under its 2022 price.

The business is split into three segments - Consumables, Capital Equipment and Disruptive Technologies, the last segment Disruptive Technologies is loss making and the company is essentially asking investors to separate these losses as they will either convert to earnings or be shut down. The market will exclude these in a bull market but include them in a bear market so until we see losses dissipating it will be included, luckily management is acting here, and losses will be curbed in the short term. The Consumables business is the largest business with sales of approximately $100m, products are sold to OEM's, Component & Consumables suppliers, laboratories, pharma companies, environmental testing companies and suppliers, pathology companies etc. Most of the products that TRJ supplies are highly specific, niche products that are complex to manufacture and clients typically have few suppliers, hence, once TRJ has a client they tend to retain and grow the client. The underlying clients have been growing at GDP plus and TRJ has managed to add sales via new products as well as M&A. The Capital Equipment business has sales of circa $60m and typically sells analytical testing equipment for a range of industries including pharmaceuticals, environmental, pathology, food testing and biological testing. The products are unique and specialised and include micro-sampling, fluid separation, blood sampling, biopsy testing etc. The clients are generally blue chip multi-national OEM's who may distribute TRJ equipment under their brand. So, what went wrong?

TRJ essentially attempted to grow too fast, or faster than the company could manage, they still need to consolidate sites and companies to extract the benefits and they have been deliberately slow, so they retain clients and IP, the pace of consolidation is picking up, but they are also getting to the end of this process. They were also subject to industry destocking, and they argue that this was expressed in the first half, clearly the market was a little bit suspicious regarding this claim. Clients built stock levels to a "Just in Case" level rather than a "Just in Time" level during COVID and as conditions normalised so did the level of stock, client's taking stock levels down by 20% had a significant impact on the half year results given that several major clients did this concurrently. There were other factors impacting the results which compounded the problem, but the share price is 25% off its peak price, we know that was wrong, but we can still see 50% upside!

***Paragon Care (PGC) – Where can you find a Micro-Cap stock with $3b in Sales!***


PGC has a bit of history, it was a rollup that failed, and the board went through successive CEO's, the company merged with a founder led distributor (Quantum Health) who appointed a corporate CEO only to fire him when costs blew out and now the company is merging with the much larger CH2. CH2 is a specialised logistics provider to the healthcare industry, initially CH2 was a pharmaceuticals wholesaler to hospitals and independent pharmacies but they have grown their distribution into a wider range of healthcare services.

PGC is a distributor of capital and consumable items to the healthcare industry focussing upon Aged Care, Hospitals, Medical Research, Universities, Specialists and cover a wide range of modalities such as ophthalmology, pathology, radiology, ultrasound, aged care, critical care etc. They distribute a wide range of capital and consumable products. Both companies utilise distribution centres across Australia and PGC has a presence in Asia as well as NZ. PGC have greater margins but CH2 has significant sales into hospitals and pharmacy where margins are paper thin but volumes super high. CH2 focus on being the lowest cost provider and this philosophy will filter through to PGC and benefits will be extracted over time. CH2 generates circa $3b in sales and PGC $330m but profits as measured by EBITDA are $54m in CH2 & $39m for PGC, the company assumes that they can find $5m of synergies which seems light given the distribution overlap, but we can get a micro-cap generating $100m of EBITDA. Some paper is being issued to CH2 shareholders but with a little growth into 2025 PGC is trading on an undemanding PER of 9.5X with a platform to grow. The stock is now trading around 30-32c and once the merger is complete, we can see it trading above 40c as the CH2 management team extract value from the merger.

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## Outlook and Strategy

Central banks seemed to have navigated a soft-landing for global economies and have managed to wrestle the inflation genie back into the bottle. Equity markets have priced in this scenario already and valuations in certain stocks and sectors of the market have reached lofty levels. The onus will be on these stocks and sectors to deliver on profits to justify these valuations. We do believe however that current conditions should set a platform for Australian small caps. We have already seen them gain lost ground over their large cap counterparts and believe this will continue over the medium term, on the proviso there are no left field surprises around the corner. Regardless, we continue to see opportunities like Trajen, Paragon Care, Veem and Acrow where we can add value to your portfolio, and we are expecting better returns into the future.

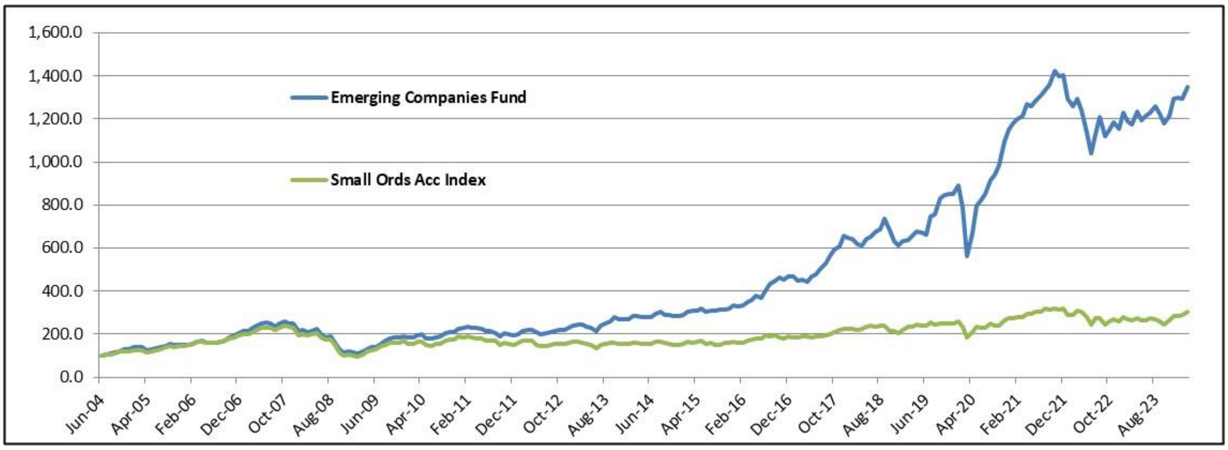
**Top 10 Holdings**

| Company Name | Portfolio % | Index % |
|---|---|---|
| Veem Ltd | 5.0 | 0.0 |
| Acrow Limited | 4.7 | 0.0 |
| IPD Group | 4.4 | 0.0 |
| Viva Leisure | 4.0 | 0.0 |
| Immutep Ltd | 3.5 | 0.0 |
| Prophecy International | 3.5 | 0.0 |
| Pacific Current Group | 3.4 | 0.0 |
| Genetic Signatures | 3.2 | 0.0 |
| IVE Group Ltd. | 3.1 | 0.0 |
| Retail Food Group | 2.9 | 0.0 |
| **Total Top 10** | **37.7** | **0.0** |

**Sector Exposure**

| Sector Exposure | Portfolio % | Index % |
|---|---|---|
| Communication | 5.4 | 4.4 |
| Consumer Discretionary | 12.7 | 16.7 |
| Consumer Staples | 0.0 | 2.6 |
| Energy | 1.8 | 7.9 |
| Financials | 8.3 | 10.1 |
| Health Care | 15.6 | 6.1 |
| Industrials | 30.7 | 8.2 |
| Information Technology | 8.3 | 6.2 |
| Materials | 13.6 | 24.4 |
| Property Trusts | 0.0 | 13.2 |
| Utilities | -- | -- |

## Growth of Emerging Companies Fund

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