PURE ASSET MANAGEMENT

Investor Newsletter
Period to 29 February 2024

PURE Income and Growth Fund

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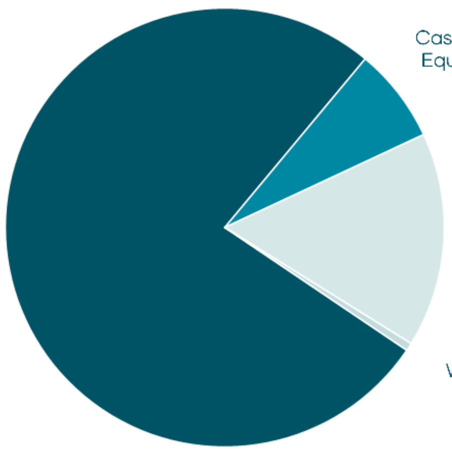
Superior SQM Research

Foundation Class Portfolio Returns (After Fees)

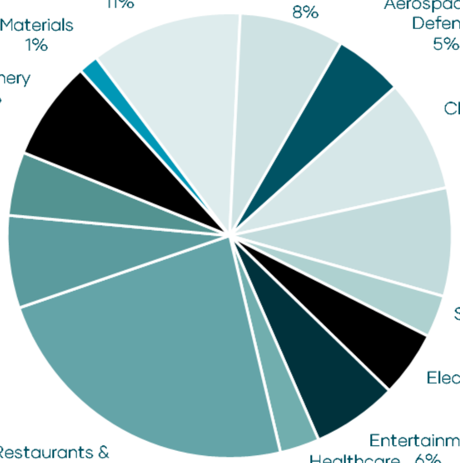
	1 month %	3 Months %	6 Months %	1 Year %	3 Years % p.a.	Since inception* % p.a.
PURE Income and Growth Fund	+0.2%	+1.2%	+2.5%	+4.6%	-0.7%	+10.4%
Standard Deviation (Annualised %)				1.1%	5.9%	11.3%
Sortino Ratio						1.3
Sharpe Ratio						0.6

** Fund inception 21 December 2018*

Portfolio Asset Allocation



Fixed Interest Sector Allocation



PURE online application form

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Fund Overview

Fund Size	$113.9m
Foundation Class Unit Price	$1.1527
Number of Investments	18
Average Loan Size	$5.4m
Weighted Average Interest Rate	10.3%
Arrangement Fees Paid to Investors	$4.0m
Trailing Fund Yield (12m)	6.3%

Monthly Commentary

Equity markets performed strongly in February, with the All-Ords Accumulation Index logging a +1.2% gain. Amid bearish positioning the corporate earnings season proved 'less bad' than consensus expectations, ultimately fuelling the rally.

Pleasingly, this extended to the under-owned small cap space as the ASX Emerging Companies Index rose +5.0% for the month. While poor liquidity exacerbated small cap underperformance in 2023, a corresponding tailwind is presented in rising markets. If markets are to trend higher in 2024, and if you subscribe to the theory of mean reversion, the stage is set for meaningful outperformance within the small-cap cohort.

The Fund rose +0.2% for the month of February. Credit performed in line with expectations, while modest equity declines were recorded across AD1, HPC, and DXN. Importantly, we are buoyant on the short-term outlook of all three companies.

This month we delve into liquidity, the ASX, its role as a mechanism for raising capital, recent performance for doing so, and what to expect going forward.

The path emerging for small-cap returns

In recent months we have built a case for the outperformance of smaller companies in 2024. While there is no perfect set of conditions to drive this, variables such as economic data, earnings and liquidity are all at play in some capacity. In isolation, these variables suggest a clear path to small-cap prosperity. While improvements in economic data and earnings expectations are pleasing, it could be argued that liquidity is the largest driver of small company performance – both to the upside and the downside. We explore this late cycle variable in greater detail below.

Economic Data: Over the past two years, global economies have digested the most aggressive round of interest rate hikes in recent history. While economies have slowed and will continue to do so, we are still here, the world is functioning, and predictions of economic Armageddon have not eventuated. With interest rate expectations now to the downside, there is cause for optimism.

Earnings: While the consumer remains under pressure (which will continue), 1H24 reporting season remained constructive. Yes, cost inflation was a common theme across all sectors, yet offsets were found in the form of cost-out initiatives and technology efficiencies. The benefit of these for savings is the extremely lean go-forward cost bases, the outcome being enhanced operating leverage to any economic recovery.

Liquidity: The one variable we would like to unpack in greater detail is liquidity. As it relates to investing, liquidity can be defined in many ways. It is not one isolated event, but multiple variables within the market cycle. The return of each liquidity variable represents progress towards improved investor confidence, on-market trading, and the release of animal spirits. We expand on these thoughts below.

- **Corporate Activity**

  In times of market dislocations, it is investors who experience fear. Inevitably, this fear is responsible for poor capital allocation decisions, ultimately destroying value in the process. Corporates, on the other hand, see depressed valuations as an opportunity. They are afforded time to make a calculated decision, conduct due-diligence, and decipher whether the purchase of a business makes strategic sense. These periods represent an opportunity to allocate capital towards pricing inefficiencies at the smaller end of the market. The emergence of corporate activity draws a line under value and is often the first step in restoring confidence.

  Anecdotally, it has been pleasing to see this theme play out during FY24. Since the financial year began there have been three takeovers within PURE's portfolio, while further activity continues. A similar theme has been experienced on the ASX, with a range of takeovers finalised at above-average premiums.

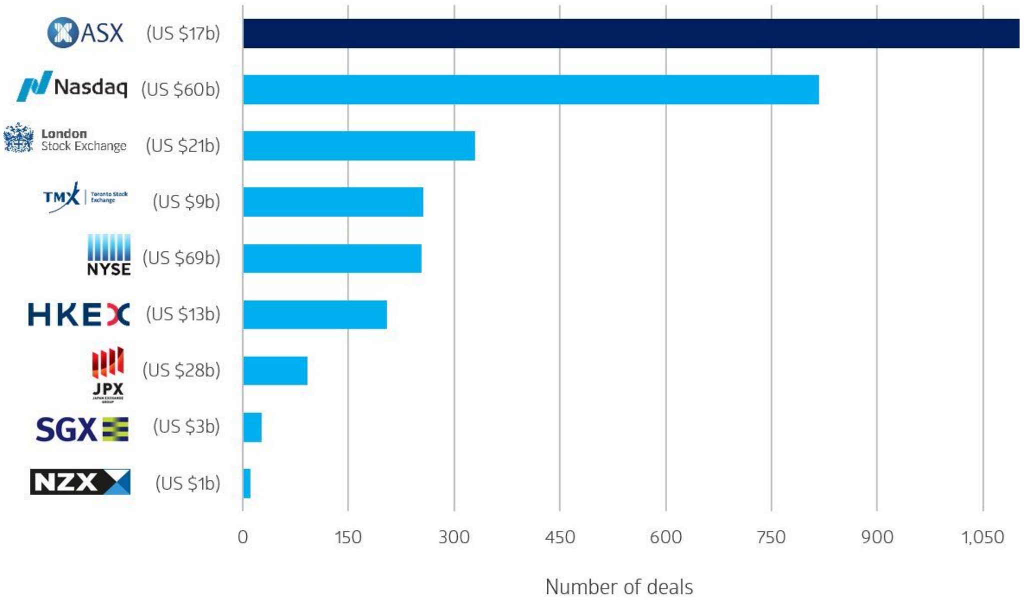
- **IPOs**

  IPOs represent an important yardstick in determining investor confidence. Unfortunately for Australia this data was stark in 2023, an unsurprising outcome in the face of economic uncertainties. 2023 saw the ASX raise $1.1bn in IPO capital across 45 listings. Within this, 66% of the capital raised related to 3 of the 45 deals. This represents a terrible 12 months for the ASX when compared to the 5-year average IPO value of $5.4b per annum.

  The recent announcement of Chemist Warehouse's pseudo-IPO (Reverse Takeover) provides cautious optimism about the IPO outlook. In general terms, the ASX has disclosed that their current listings pipeline points to an increase in 2024 IPO activity. The return of the IPO market represents a step towards improved sentiment, a willingness to do business, and a reason to remain cautiously optimistic on the broader return of liquidity.

- **Secondary Market Raisings**

  While the ASX IPO machine spluttered in 2023, equity raising more broadly remained intact. The ASX raised ~US$17b in equity throughout 2023 across c.1,100 deals (see chart below). Of surprise to us was the sheer quantum of deals and where this positioned the ASX relative to global peers. The ASX finished 2023 with the most equity raises of any exchange globally, placing fifth by dollar value.



While valuations are not where smaller ASX companies would like them, markets remain open for business. Capital should remain available for sustainable businesses seeking growth funding, yet we expect corporates to remain price takers in the immediate term.

- **On-market Trading**

While listed as the fourth 'liquidity variable' given it's late-cycle nature, on-market trading is arguably the most important driver of small-cap equity performance. Simplistically, it can be argued that recent small-cap equity underperformance was driven by more sellers than buyers. The second derivative is that poor liquidity facilitates an outsized equity valuation divergence relative to underlying operational performance. Smaller companies have experienced this downdraft in recent periods, yet as we like to say, 'the punishment doesn't always fit the crime'.

We now consider a comparative upside opportunity in place. For upside to eventuate, investors must first lower their eyes to each individual micro-cap opportunity. With interest comes trading, with trading comes liquidity. Based on current valuations and interest levels, the return of investor interest and liquidity should see share prices squeeze higher in response.

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Thank you

Nick, Mike, Tim, Dan, Jonathan and Jean-Luc

Monthly Returns – After Fees

The Income and Growth Fund – Foundation Class													
Year	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Fin YTD
FY19						2.4%	-1.8%	1.2%	0.3%	-1.0%	2.5%	1.7%	5.4%
FY20	2.6%	-1.4%	2.1%	1.4%	-0.8%	3.8%	2.8%	-2.2%	-3.8%	3.8%	5.7%	0.7%	15.0%
FY21	15.9%	8.8%	-1.0%	12.2%	0.7%	2.6%	-1.0%	-1.0%	-3.5%	2.1%	0.0%	0.8%	40.9%
FY22	3.4%	-3.2%	2.3%	1.2%	-2.2%	1.0%	-0.1%	-2.3%	1.6%	0.5%	-0.5%	-1.0%	0.5%
FY23	1.3%	-1.7%	-1.6%	0.9%	-5.7%	0.1%	0.2%	0.3%	0.2%	0.1%	0.4%	0.3%	-5.3%
FY24	0.5%	0.5%	0.7%	0.0%	0.7%	1.1%	-0.1%	0.2%					3.6%

The Income and Growth Fund – Platform Class (APIR: PUA7226AU)													
Year	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Fin YTD
FY21	16.0%	8.9%	-0.9%	12.4%	0.7%	2.7%	-0.9%	-1.0%	-3.5%	2.1%	0.0%	0.8%	41.8%
FY22	3.4%	-3.2%	2.3%	1.2%	-2.2%	1.0%	-0.1%	-2.3%	1.6%	0.5%	-0.5%	-1.0%	0.5%
FY23	1.3%	-1.7%	-1.6%	0.9%	-5.7%	0.1%	0.3%	0.3%	0.2%	0.1%	0.5%	0.3%	-5.3%
FY24	0.5%	0.5%	0.7%	0.0%	0.7%	1.1%	-0.1%	0.2%					3.6%

Unit Price Data Download

Please click on the link below to download the updated unit price data for each unit class.

[The Income and Growth Fund – unit price data to 29 February 2024]