CV Capital Pty Ltd

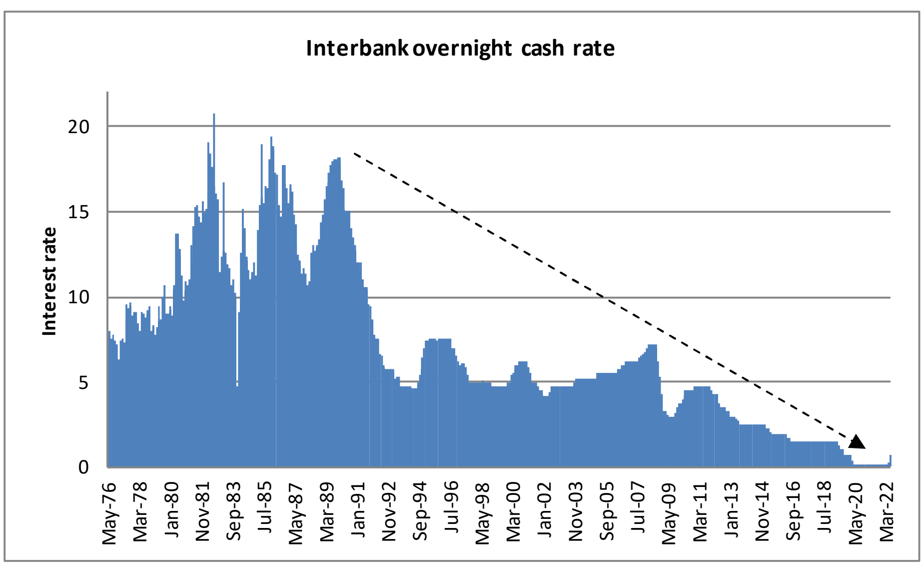
8 September 2022

SHAREHOLDER REPORT AS AT 30 June 2022

To my fellow shareholders & partners,

I have to apologise for the untimely manner of this report. My original intention was to push for completion of our financial statements (which I have recently emailed to all shareholders) by early August and disclose the share price based on the financial statements but was unable to do so due to various factors. Next year I will revert back to reporting the indicative June share price and performance in July which may be updated once our accountant finalises the financial statements.

Between the end of March and 30 June 2022, the ASX 200 index fell 12.4% which was quite significant. The US markets led the global downturn as the Federal Reserve started hiking interest rates in March and moved more aggressively in May and June in response to US inflation hitting 9.1% in June 2022. The RBA responded to inflationary pressures by hiking the cash rate in May and June by 25 basis points and 50 basis points respectively. These increases marked the end of a 30 year downward trend in interest rates which started in the late 80s and hit a low of 0.1% during the pandemic. Given the cyclical nature of the economy, one may be tempted to speculate that we could be entering a new long term upward phase in interest rates, time will tell.

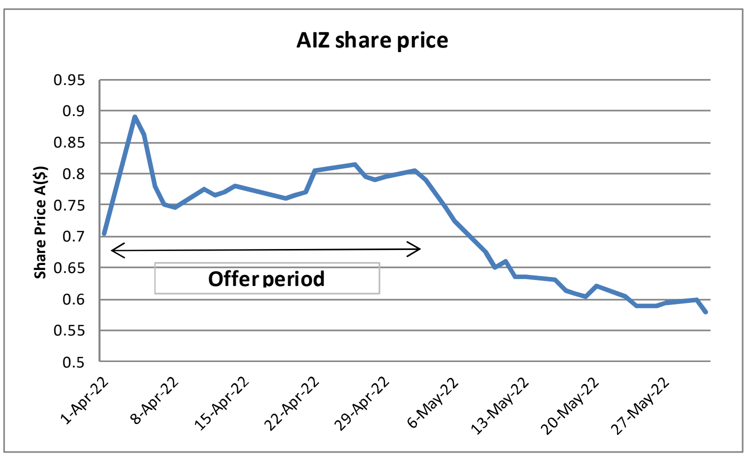


Fund Activity

During the market selloff, we added to our Baby Bunting position. The company's growth trajectory is on track with its store footprint expected to roughly double over the next 10 years and profit margins are also improving as a result of its dominant market position and expansion of its private label products. That's the good news.

The bad news is that I made a very dumb trade which resulted in a 3.7% loss (pre-tax) for the fund. In May, we invested in the Air New Zealand (AIZ) rights offer. This was a very large rights offer which raised NZ$1.2 billion and tripled the number of AIZ shares on issue. The rights issue was underwritten and had an oversubscription component, which in the event the rights were not fully taken up, existing shareholders could subscribe to those undersubscribed shares alongside institutional shareholders where a bookbuild process would set the price.

The rights issue was priced at A$0.49 and the offer period was from 5 April 2022 to 2 May 2022. AIZ was trading at circa A$0.70 before the announcement of the capital raising and one would have expected to see the share price fall closer to the rights issue price after the announcement of such a large dilutive capital raise. However, if you look at share price chart below AIZ shares continued to trade significantly above the rights issue price during the offer period. The average share price throughout this offer period was circa 78 cents which was a 59% premium above the rights issue price.

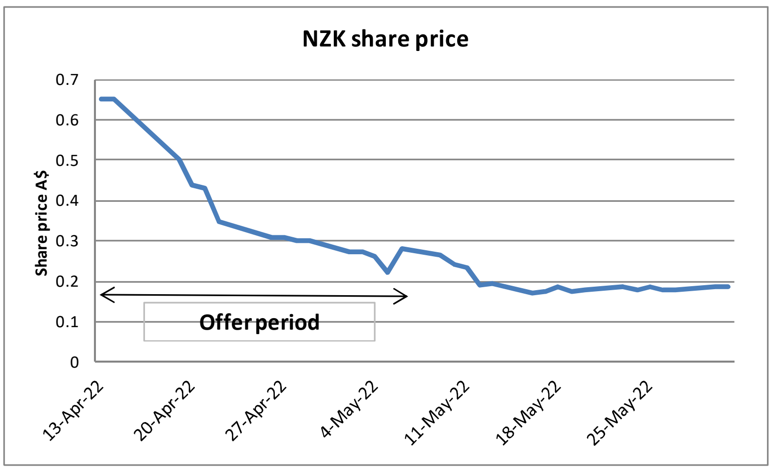


This trade looked appealing given the size of the premium and the oversubscription component which was not capped. While the oversubscription component did involve a book build which created the risk of an unknown share price for the undersubscribed shares at the time of application, logic would suggest that the participants of the book build would unlikely pay a huge premium above the rights offer price given the quantum of the new shares being issued that would certainly put pressure over the share price in the short to medium term. Moreover AIZ operated in a tough industry devastated by Covid and had a history of losses.

So we invested in the oversubscription portion of the offer as I figured the odds were good given the large premium (AIZ share price was still trading at A$0.80 - 63% premium at the end of the offer period) and planned to make a quick profit. We ended up receiving about 2/3 of our oversubscription application but ended paying A$0.74 per share after the bookbuild process was completed, a whopping 51% premium above the rights issue price which eliminated most of the "premium" to the share price. I still find it strange that there was such strong demand from investors which drove up the oversubscription price from $A0.49 to A $0.74 given 1) the quantum of shares being issued at A$0.49 cents and 2) AIZ poor history of long term profitability.

At market open following the bookbuild, the shares opened at A$0.74 and very quickly fell from there given the selling pressure from all the new shares issued at the A$0.49 cents rights issue price. By the time we managed to sell all our shares, we lost circa 27% on this trade.

Contrast the AIZ share price behavior with another capital raising during the same period. New Zealand King Salmon (NZK) also did an equally dilutive rights offer during the same period which was underwritten and had an oversubscription option which was capped. The rights offer was priced at NZ$0.15/ A$0.138 per share and the offer period was between 13 April 2022 and 6 May 2022. We can take a look at NZK share price movement and compare it to the AIZ share price movement during and after the offer period.



A day before the capital raising announcement, the share price was A$0.65 and at the close of the offer period, it had fallen to A$0.28 cents, a 57% decline which is common for highly dilutive rights issues priced significantly below the share price. Contrast this with AIZ where during the offer period, rather than falling towards the rights issue price, the share price appreciated from A$0.705 to A$0.805.

With hindsight, it's easy to see that the AIZ capital raise had to succeed given it involved a national carrier and was such a crucial capital raise for the company. Given the huge sums involved and the risk to the underwriter and the NZ financial markets if the offer was massively undersubscribed, I believe the stakeholders were artificially supporting the share price during the offer period which helped entice shareholders to subscribe. In the end the capital raise was a success and once the share price support was withdrawn (after the offer closed), the share price fell very quickly.

I've learnt an expensive lesson here and hope to be smarter in the future.

Fund Performance

CV Capital's return for FY2022 (1 Jul 21 – 30 June 22) is -0.2% (before prior period's performance fees) and -2.3% (after prior period's performance fees). Since inception our returns are 11.9% (before performance fees) and 11.3% (after performance fees) on an annual compounded basis. Our benchmark's return for FY2022 was -6.8% which are inclusive of dividends and franking credits distributions. For the purposes of assessing the performance fees I have mistakenly calculated the benchmarks performance as -6.4% (Note 1C of the FY2022 financial statements) which is better than actual and resulted in a smaller performance fee. Given it was my mistake and the financial statements have been finalised, I've decided to not make a correction.

If you refer to the profit and loss statement in our FY2022 financial statements, you will see that we made an unrealised loss for the year which is basically a fall in the quoted market price of our securities portfolio. Our portfolio values fell alongside the share market selloff this quarter. However, these unrealised losses for FY2022 were offset by the dividend received and profit from disposal of investments. Most of the profit from disposal of investments came from our arbitrage trading activities which greatly contributed to the portfolio performance in FY2022. These arbitrage trades do not involve huge risks as they take advantage of price differences in dual listed securities.

On performance fees/ bonus, although the fund has beaten the benchmark for FY2022, I do not like taking a performance fee when the performance of the fund was negative for the year. Therefore, I've decided to withhold the payment of my performance fees for FY2022 until the fund registers a positive return measured from 1 July 2021.

Dividends and reinvestment price

Similar to prior year, we will be issuing a dividend for the sole purpose of distributing the franking credits to our shareholders. Franking credits have no value in the fund and our shareholders may be able to benefit from it depending on your individual tax position. Given the aim of the fund is to compound capital for the longest possible period, by default I will be reinvesting the dividend into the fund and urge all of you to do the same. If you do not wish to reinvest your dividends, please advise me soonest possible.

For FY2022, the fund will be issuing a fully franked dividend of **11.03 cents** per share which will be paid in the next 2 weeks. A dividend statement will be issued to all shareholders.

The reinvestment price based on the June 22 share price verified by our accountant is calculated below:

Based on FY2022 financial statements	Per share
Net assets	$1.34
Add: Franking credits	$0.05
Add: Current tax liabilities (realised gains)	$0.03
	$1.42
Less: Tax liabilities on unrealised gains	($0.02)
Less: Performance bonus	($0.02)
Less: Dividends declared (incl. franking credits)	($0.16)
Reinvestment price (rounded)	**$1.22**

YOURS SINCERELY,
DARRELL CHEAH