

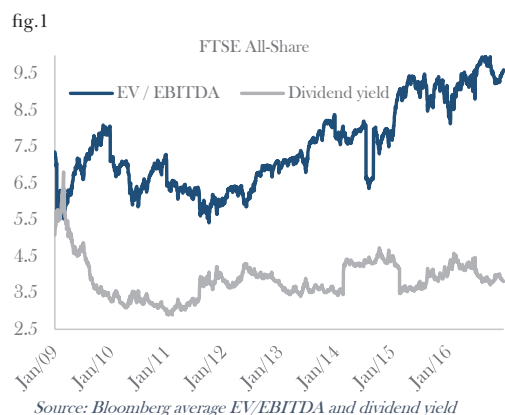


“Smaller companies with value characteristics set to outperform”

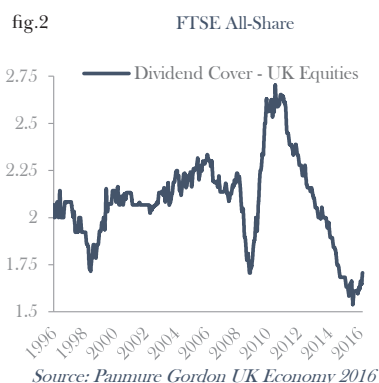
- 1) Markets are expensive, adopting a nautical analogy, we are approaching ‘spring tide’
- 2) We believe the rotation out of growth stocks into those with ‘value’ characteristics will continue to gain traction throughout 2017
- 3) The opportunity is at the smaller end of the market where valuation dislocation opportunities exist

Current valuations are relatively high

The FTSE All-share is trading on an EV/EBITDA multiple of c.10x, having been as low as c.6x in 2009 (fig.1).



Dividend yields have fallen significantly from around 6% in 2009 following the financial crisis and are now 3.75%, however it is important to note that dividend cover has fallen sharply since 2010 (fig.2).



We are not necessarily suggesting the market will fall in the near-term because reflationary pressures could support continued growth however ‘ships on a rising tide’ springs to mind.

Value stocks to outperform

We believe now is the time to be rotating into stocks that are intrinsically undervalued rather than the momentum/quality focus of the last 5 years.

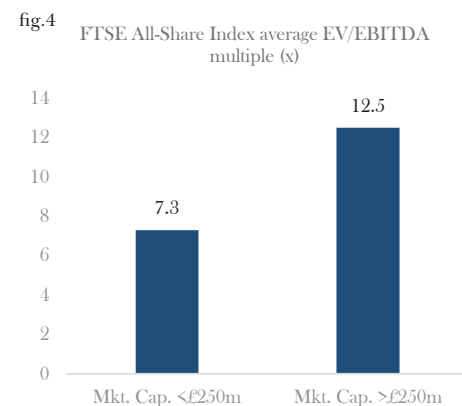
Investors should focus on companies that generate healthy cash flows and produce good return on capital - ‘value stocks’ that have been significantly overlooked.

In our H1 2016 Investment Perspectives, we highlighted the value/growth opportunity. We have begun to see this rotation into value gain traction towards the end of 2016 and into this year.



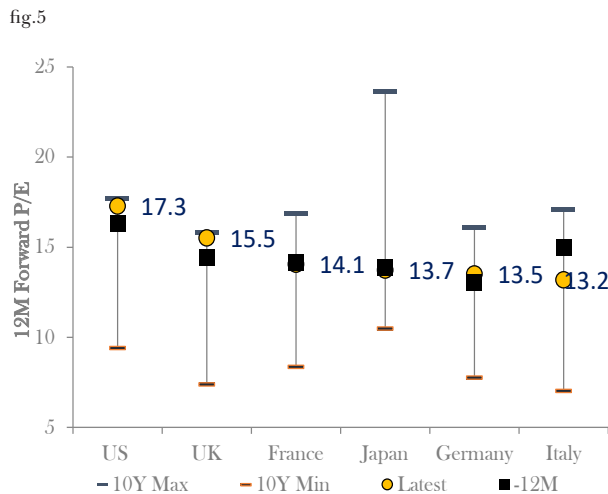
The bifurcation in the markets between highly valued, larger more liquid companies and lowly valued smaller companies remains.

The difference in valuation between the larger and smaller stocks in the FTSE All Share Index is significant with the average prospective EV/EBITDA multiple for those companies above £250m market capitalisation of 12.5x vs 7.3x for those below £250m (fig.4).



Source: Bloomberg, 13th Jan 2017

We believe the valuation discount for UK smaller companies provides an opportunity to generate superior long term investment returns. The FTSE All-Share is trading at the upper end of historic ranges at c.15x PER (fig.5).



Source: Panmure Gordon UK Economy 2016

This has been driven by re-rating rather than earnings growth and upgrades, with companies benefiting from low cost of capital, quantitative easing and weaker sterling.

Against an uncertain political and economic backdrop globally we believe such ratings will be hard to sustain. Many corporates are operating at margins and levels of profitability pre financial crisis¹, which could come under pressure if we begin to see wage inflation, and increased cost of borrowing.

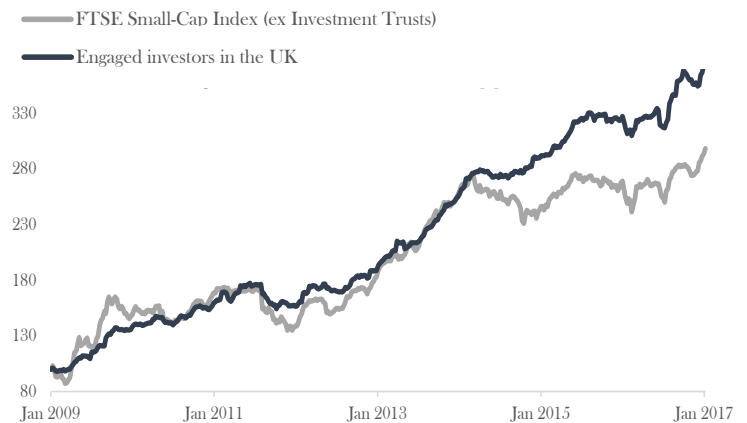
We believe stock picking will be critical and investors should focus on those companies that can identify catalysts through either operational improvement, restructuring or strategic initiatives to create shareholder value over the long-term.

1, Panmure Gordon Q1 2017 Economic Almanac

Engagement can be critical when investing in smaller companies.

Active investing has come under criticism by the FCA recently with analysis concluding that after fees the returns over or above passive strategies are marginal. But where investors are prepared to spend time and engage or support management teams, take influential stakes and 'roll up their sleeves' to add value, there is scope for superior returns over the long term.

We have run the average NAV performance of known engaged investors in the UK relative to the FTSE Small-Cap Index below which in the main arrives at the same conclusion.



Source: Bloomberg. Tracking avg NAV growth for engaged investors (basket of North Atlantic Smaller Companies plc, Strategic Equity Capital plc, Crystal Amber plc and Gresham House Strategic plc since Aug 2013) vs the FTSE Small-Cap Index (excluding Investment Trusts)

Adopting a nautical analogy, we are approaching 'spring tide'.

Investors should focus on good quality companies that are lowly valued and where shareholder returns can be identified from either earnings growth, multiple expansion or excess cash generation and where earnings growth can be improved - moving away from those operating at peak margins and at the upper end of historic valuation multiples.

Jonathan Dighe

Commercial Director, Gresham House Plc

T. 020 3837 6273 E. j.dighe@greshamhouse.com

W. www.greshamhouse.com

IMPORTANT INFORMATION This strategy document (the "document") is issued by Gresham House Asset Management Ltd ("GHAM") a 100% subsidiary of Gresham House plc (GHE), for information purposes only. Its contents and any information provided may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, in whole or in part, for any purpose, without the consent of GHAM. Acceptance of delivery of any part of the document by you constitutes unconditional acceptance of the terms and conditions of this notice. This document does not itself constitute an offer to subscribe for or purchase any interests or other securities. It is not intended to be relied upon as the basis for an investment decision, and is not, and should not be assumed to be, complete. It is provided for information purposes only. Any investment is subject to various risks, none of which are outlined herein. All such risks should be carefully considered by prospective investors before they make any investment decision. You are not entitled to rely on this document and no responsibility or liability is accepted by GHAM, GHE or any of its directors, officers, partners, members, employees, agents or advisers or any other person for any action taken on the basis of its content. No undertaking, representation, warranty or other assurance, express or implied, is made or given by or on behalf of GHAM, GHE or any of its respective directors, officers, partners, members, employees, agents or advisers or any other person as to the accuracy or completeness of the information or opinions contained in this document and no responsibility or liability is accepted by any of them for any such information or opinions. Past performance is not indicative of future results. The value of investments may fall as well as rise and investors may not get back the amount invested. Changes in rates of foreign exchange may cause the value of investments to go up or down. No representation is being made that any investment will or is likely to achieve profits or losses similar to those achieved in the past, or that significant losses will be avoided. Prospective investors should seek their own independent financial, tax, legal and other advice before making an investment decision. Statements contained in this document that are not historical facts are based on current expectations, estimates, projections, opinions and beliefs of GHAM. Such statements involve known and unknown risks, uncertainties and other factors, and undue reliance should not be placed thereon. In addition, this document contains "forward-looking statements." Actual events or results or the actual performance of the Fund may differ materially from those reflected or contemplated in such forward-looking statements. Certain economic and market information contained herein has been obtained from published sources prepared by third parties and in certain cases has not been updated to the date hereof. While such sources are believed to be reliable, neither GHAM, GHE nor any of its directors, partners, members, officers, employees, advisers or agents assumes any responsibility for the accuracy or completeness of such information. No person, especially those who do not have professional experience in matters relating to investments, must rely on the contents of this document. If you are in any doubt as to the matters contained in this document, you should seek independent advice where necessary. This document has not been submitted to or approved by the securities regulatory authority of any state or jurisdiction. For the Attention of United Kingdom Investors This document is intended for distribution in the United Kingdom only to persons who: (i) have professional experience in matters relating to investments, who are investment professionals, high net worth companies, high net worth unincorporated associations or partnerships or trustees of high value trusts, and investment personnel of any of the foregoing (each within the meaning of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005). For the Attention of Investors outside the United Kingdom This document relates to an Alternative Investment Fund within the meaning of the Alternative Investment Fund Managers Directive and the availability of this document will be subject to registration in relevant jurisdictions as described in the documents relating thereto. Any dissemination or unauthorised use of this document outside the United Kingdom by any person or entity is strictly prohibited.