

LF Gresham House UK Micro Cap Fund

Factsheet commentary – July 2023

Past performance is not necessarily a guide to future performance. Portfolio investments in smaller companies typically involve a higher degree of risk. Capital at risk. Extracted portfolio performance is not necessarily indicative of the performance of the fund. Not to be construed as investment advice or recommendation. Views expressed by the investment team are correct at the time of writing but are subject to change.

Overview

Following disappointing performance in June, UK equity indices recovered in July with the FTSE 100, 250, Small Cap and AIM All Share indices all delivering low single digit returns in the month, bolstered by a better-than-expected improvement in UK inflation. Despite the year to date 'de-equitisation' of UK markets following elevated levels of takeover activity and equity fund outflows, July saw the first "sizeable" UK IPO in 2023, which should hopefully act as a sign of confidence in the UK equity market outlook. However, macro uncertainty continues to weigh on investor sentiment, with a number of indicators (e.g. PMI, consumer confidence) pointing towards economic challenges.

Despite the challenging environment, we remain confident that our portfolio of businesses has strong fundamental and sustainable income characteristics, with most companies exposed to resilient structural growth trends or self-help opportunities and therefore able to perform well despite the wider macroeconomic uncertainty.

News flow across our portfolio companies has on the whole been positive and well received by the market, with a number of trading updates demonstrating better than expected financial performance. In the year to date, c.85% of portfolio company updates have been in-line or positive relative to market expectations.

The longer term discounted valuations applied to UK equities, and in particular the smaller companies segment, remains material. Building on the strong momentum in UK plc takeover announcements in the first half of this year, several further takeover announcements followed in July, including the Recommended Offer for DWF Group plc by Inflexion Private Equity.

Performance¹

The LF Gresham House UK Micro Cap Fund increased by 0.72% during the month, underperforming the IA UK Smaller Companies sector which increased by 1.51%.²

Key contributions came from **Kooth** (+41%) following the announcement of the minimum contract value for its transformational Californian contract, which has more than doubled FY24 revenue forecasts; **Diaceutics** (+21%) following a well-received H1 trading update which confirmed a strong start to the year, with a record orderbook de-risking FY23 and beyond; and **Angling Direct** (+15%) on no specific news.

1. Please refer to the factsheet for full NURS-compliant performance figures.

2. The IA UK Smaller Companies sector comparator is used for illustrative purposes only.

The largest detractors to performance were **Franchise Brands** (-21%), despite interim results indicating a strong start to the year, with FY23 EBITDA expected to be 'at least' in line with market expectations; and **Netcall** (-10%), which released a trading update confirming a strong close to FY23, however also indicated a renegotiation on the timing of a contract, which led to marginal changes to outer-year forecasts.

Portfolio activity

There were no new investments during the period.

We made selective follow-on investments during the period, including into **Kooth**, a digital mental health company, as part of a £10mn equity placing which was launched alongside the announcement of its significant Californian contract, to ensure the Company has the firepower to execute on its growth strategy; and **Trufin**, a group comprising four separate businesses operating across software and niche lending solutions, alongside video game publishing, which the Manager continues to view as undervalued on a sum-of-the-parts basis.

We exited **Medica** (+44%) during the period following the completion of a takeover from IK Partners, a European private equity firm.

Outlook

We continue to expect that market conditions will remain volatile throughout the remainder of 2023, with a particular focus on the UK's inflation trajectory and implications for, inter alia, the monetary policy path. However, the Fund remains well positioned, with a portfolio of relatively resilient businesses, exposed to structural growth trends and with strong fundamental characteristics that we believe should perform well through the cycle.

While we view the outlook with suitable caution, we expect heightened volatility to drive attractive long-term investment opportunities and we remain vigilant for evidence of mispricing. We remain selective and disciplined in our approach, seeking high-quality companies with attractive long-term structural capital growth at sensible valuations.

Building on the elevated levels of takeover activity in the year to date, we expect to see further activity amongst listed UK companies throughout the remainder of the year, as corporate and private equity buyers seek to benefit from the ongoing dislocation between strong company fundamentals and UK equity valuations. Significant levels of capital yet to be deployed by private equity firms could continue to provide a supportive landscape for elevated corporate activity over the short to medium term.

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