Since 1857 Gresham House Specialist asset management

WS Gresham House UK Smaller Companies Fund

Factsheet commentary – December 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 a recommendation. Views expressed by the investment team are correct at the time of writing but are subject to change.

Overview – Q4 2023

UK equity markets entered Q4 2023 with the Bank of England base rate at 5.25%, the highest level in 15 years. While surprise disinflation and base rate stability provided positive signals, market performance in September was broadly flat. In October, UK stock market indices declined as emergent geopolitical instability in the Middle East intensified global uncertainty. This theme persisted throughout the quarter, most recently as attacks on commercial ships in the Red Sea pushed freight costs higher. However, continued reductions in headline inflation and stable base rates supported a rebound in UK equity performance during November and December; the FTSE 350 rallied by 7.0% and the FTSE AIM All Share Index by 12.3%, with markets pricing in expectations of continued moderating inflation and falling interest rates in 2024.

During this volatile period M&A activity across the UK market remained elevated, especially at the smaller end of the market-cap spectrum, further evidencing the steep valuation discount currently applied to UK smaller companies versus comparable M&A transactions.

We operate under the assumption that the economic and geopolitical uncertainties which characterised Q4 2023 will continue to drive periods of market volatility. Nevertheless, we are confident in the strong fundamentals of our portfolio companies and their ability to navigate external headwinds. Particularly, we focus on businesses with quality management teams who pursue clear growth strategies in structurally growing markets and those which benefit from strong competitive positions and robust financial profiles. As a result, we think our portfolio companies can continue to grow earnings and generate attractive cash flows throughout the cycle.

Newsflow across the portfolio was largely positive in Q4 2023, as several companies delivered positive trading updates or made acquisitions which were well-received by the market. As an indicator of portfolio quality and resilience, c.85% of company updates in the fund have been in-line or positive relative to market expectations during 2023.

Performance[1]

Performance in the WS Gresham House UK Smaller Companies Fund increased by 7.1% during the month, outperforming the IA UK Smaller Companies sector which increased by 7.0%.[2]

---

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

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

Key positive contributions came from **Smart Metering Systems** (+47%), following a recommended cash offer from US private equity group KKR, at a 40% premium to prior day close; **Elixirr (**+30%) following the acquisition of US consultancy firm Insigniam, which enhances the group's position in the US market following two previous US acquisitions; and **Ten Entertainment** (+35%) following a recommended cash offer from Trive Capital at a 33% premium to prior day close.

The largest detractors to performance were **Tribal Group** (-17%) following publicly announced opposition from a large shareholder to the recommended cash offer by Ellucian; **Moonpig** (-13%) despite the release of in-line interim results reporting significant progress on both strategic and financial initiatives; and **Brooks Macdonald** (-6%), on no specific news.

Portfolio activity

There were no full exits or new investments during the period.

We made several selective follow-on investments, including into **Halfords,** as we believe the current rating fails to reflect the recent strategic progress made in repositioning the business further towards its service offering, nor the significant self-help levers that are delivering cost savings; **Alpha FMC**, a challenger consultancy firm primarily focused on financial services which continues to execute on its growth strategy and demonstrate resilience, despite broader market headwinds; and **Team17**, an independent video game developer and publisher; following an unexpected profit warning in November and subsequent review, we believe the long-term fundamentals of the business remain strong and that the current reduced share price offers an attractive opportunity to add to the Fund's position.

Outlook – Q1 2024

While global markets price in expectations of easing inflation and falling interest rates in 2024, we do not expect market volatility to abate given the ongoing macroeconomic and geopolitical uncertainty. We believe that present conditions will continue to generate mispricing opportunities across the UK market, particularly across the smaller companies segment, yet we are conscious to retain a sharp focus on resilient businesses with high-quality fundamentals.

The UK markets de-rated through 2023, with many companies continuing to trade at a stark discount to history, as well as versus international and private peers. As market valuations remain low it is worth considering that in in some cases de-ratings may be warranted. Through 2023 we saw elevated profit warnings across the UK market, a trend which we expect to continue into 2024, therefore some companies may not be as attractively valued as they initially seem and hence, we view this as a stock-pickers market. We continue to leverage our network to glean unique expertise and analytical insights, helping us validate and build conviction across discrete components of our investment theses. Using this advantage in tough market conditions navigates us away from 'value traps' which tend to appear in a 'cheap' market, allowing us to focus our deployment into high quality businesses, trading at attractive valuations.

We also expect M&A activity to persist into early 2024 as UK equities remain heavily discounted relative to comparable M&A transactions. In the US and Europe, mid-to-large leveraged buyout firms are looking to offset the higher cost of debt by purchasing UK listed businesses at steep discounts to intrinsic value. The evidence from 2023 suggests that the private equity gaze is firmly fixed on UK smaller companies, where the discrepancy between trading multiples and company fundamentals appears most prevalently. As the M&A activity continues, we cautiously expect investors to bridge the gap between stock market valuations and UK company fundamentals.

Important information

The information contained in this document (the Document) is being communicated in the United Kingdom for the purposes of section 21 of Financial Services and Markets Act 2000 and has been issued by Gresham House Asset Management Limited (GHAM or the Manager). GHAM whose registered office is at 5 New Street, London, EC4A 3TW is a company authorised and regulated by the Financial Conduct Authority (FCA) (no.682776). The information should not be construed as an invitation, offer or recommendation to buy or sell investments, shares, or securities or to form the basis of a contract to be relied on in any way. GHAM provides no guarantees, representations, or warranties regarding the accuracy of this information. No third-party liability is accepted by GHAM, its members and employees, or its affiliates and their directors, in respect of errors and omissions, other than under the duties and liabilities of the Financial Services and Markets Act 2000. Potential investors are advised to independently review and/or obtain independent professional advice and draw their own conclusions regarding the economic benefit and risks of investing in the securities and legal, regulatory, credit, tax, and accounting aspects in relation to their particular circumstances. The recipient should consult its tax, legal, and accounting or other advisers about the issues discussed herein and shall be solely responsible for evaluating the risks and merits involved in the content of this Document.

This Document is provided for the purpose of information only and before investing you should read the Prospectus and the Key Investor Information Document (KIID) as they contain important information regarding the Fund, including charges, tax and fund specific risk warnings and will form the basis of any investment. The Prospectus, KIID and application forms are available from Link Fund Solutions, the Authorised Corporate Director of the Fund (Tel. No. 0345 922 0044). Investors are reminded that past performance is not indicative of future results.

Funds investing in smaller companies may carry a higher degree of risk than funds investing in larger companies. The shares of smaller companies may be less liquid than securities in larger companies.

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. This Document is intended for distribution in the United Kingdom only. Any dissemination or unauthorised use of this Document outside the United Kingdom by any person or entity is strictly prohibited.

Please contact a member of the Gresham House team if you wish to discuss your investment or provide feedback on this presentation. Gresham House is committed to meeting the needs and expectations of all stakeholders and welcomes any suggestions to improve its service delivery.

www.greshamhouse.com | (0) 20 7382 0999