Gresham House
Specialist asset management

LF Gresham House UK Micro Cap Fund

Factsheet Commentary - May 2021

Overview

The strong market conditions that have so far characterised 2021 continued during May with robust share price performance across the market. This environment continues to support both active equity issuance and elevated levels of takeover activity. Despite some increased uncertainty over the lockdown relaxation timetable in the UK, the increasing vaccine penetration looks well set to support a rapid economic recovery.

The discounted valuation applied to the UK and to UK smaller companies in particular remains material but has finally started to contract with positive flows returning to UK equity funds. May delivered one of the strongest periods of net inflows to UK smaller company funds on record suggesting that investors are starting to recognise the valuation anomaly which should continue to be supportive to smaller company share prices.

This dynamic environment continues to offer a number of investment opportunities. We remain selective and disciplined in our approach, seeking high quality companies with attractive long-term capital growth characteristics at sensible valuations.

Performance

The Fund delivered a return of -0.3% during the month, compared to the IA UK Smaller Companies sector which increased by 2.3% and the NSCI + AIM (ex IC) index which rose by 1.3%.

Key contributions to returns came from **Alpha Financial Markets Consulting** (+14%) which announced an oversubscribed placing and a strategic acquisition in the US market, adding capability in the area of alternatives with a strong roster of blue chip clients; **Kape Technologies** (+15%) which rallied after being included in the MSCI UK Smaller Companies index; and **Gym Group** (+9%) after indicating strong early trading following its sites reopening.

The largest detractors to performance were **Accrol** (-26%) after downgrading near term forecasts due to commodity price inflation despite stronger than expected synergies being achieved from its recent acquisition; **Staffline** (-14%) which announced a material placing at a discount in order to strengthen its balance sheet; and **Loungers** (-8%) which de-rated on no specific news.

Portfolio activity

During the period we made a new investment in to **Marshall Motor Holdings**, an automotive dealership group. We also made a number of follow-on investments into our existing portfolio holdings including **Staffline**, **Alpha Financial Markets Consulting**, **Filta Group**, **Argentex** and **Instem** amongst others.

We made a partial realisation, to take profits, from our holding in **Kape Technologies** following strong share price performance although it remains a core portfolio holding.

Outlook

We continue to expect a strong economic recovery in the UK during the remainder of 2021 driven by vaccine penetration supporting relaxed restrictions. Nevertheless, the extreme uncertainty that has hung over many sectors and companies makes visibility supporting market estimates unusually low. This means we expect elevated levels of profit warnings, both positive and negative as companies recalibrate expectations over the course of the year. We are already seeing many examples of both during recent weeks. This is likely to drive heightened volatility at the individual stock level. However, we believe that volatility, while creating some challenges, will provide an attractive environment in which we can unearth good long-term investment opportunities at attractive valuations. The economic environment and lingering Covid-19 discontinuity will provide agile, smaller businesses with strong management teams the opportunity to take market share and build strong long-term franchises.

We continue to believe that our fundamental focused investment style has the potential to outperform over the long term. The Fund will maintain its focus on building a high conviction portfolio of less cyclical, high quality, niche growth businesses which we believe can deliver strong returns through the market cycle regardless of the performance of the wider economy.