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LF Gresham House UK Multi Cap Income Fund

Factsheet Commentary - June 2021

Overview

Market conditions remained positive in June, rounding off a very strong period for UK equities and UK smaller companies in particular throughout the first half of the year. The dealflow environment remains extremely active. There continues to be a steady stream of IPOs and a strong pipeline for the second half although anecdotal evidence of some flotations failing to get away suggests there may be some deal fatigue setting in due to the sheer volume of equity issuance so far in 2021. There is also ongoing secondary issuance by existing listed companies to support acquisitions and growth initiatives as confidence in the vaccine driven recovery gathers pace. A number of our portfolio companies have raised new capital so far this year.

As we have been flagging for some considerable time, the discounted valuation applied to the UK and to UK smaller companies in particular remains material. This is still the case despite the strong performance during H1 2021. Some sustained positive flows are now being seen into UK funds which is an encouraging signal of improving sentiment towards the UK and should be supportive for share prices.

Large amounts of “dry powder” in private equity funds, combined with still discounted valuations, has triggered a frenzy of takeover activity in the UK equity market ranging from small caps right through to the FTSE 100. This represents a double-edged sword for investors who benefit from a short-term share price uplift but then may lose out on the long-term potential of good quality companies that leave the public markets.

The current dynamic market 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 sustainable income streams and structural capital growth characteristics at sensible valuations.

Performance

The Fund increased by 1.4% during the month, compared to the IA UK Equity Income sector which fell by 0.6% and the FTSE All Share index which fell by 0.03%.

Key positive contributions came from **Inspired Energy** (+27%), following an encouraging trading update; **Morrison Supermarkets** (+33%), after receiving an unsolicited offer by private equity firm **Clayton, Dubilier & Rice** that was rejected by the Board; and **Property Franchise Group** (+13%), which announced a strong trading update for the first five months of the year to May 2021.

The key detractors were **Vectura Group** (-13%), which was a reflection of the stock going ex-dividend; **Ricardo** (-11%), which drifted on no specific news; and **Vianet Group** (-9%), which announced full year results.

Portfolio activity

During the period, the Fund made a follow-on investment into existing holdings **Inspired Energy** and **Watkin Jones**. We also supported our existing investment **Mattioli Woods** in its equity placing to fund the strategic acquisitions of Ludlow and Maven to enhance its advisory and asset management activities.

Outlook

We continue to expect a strong economic recovery in the UK during the second half of 2021 driven by vaccine penetration and restrictions being removed later this month. Nevertheless, the extreme uncertainty that has hung over many sectors and companies is still limiting short-term visibility. In turn this will drive elevated profit warnings, both positive and negative as the year progresses.

In this context we anticipate heightened volatility at the individual stock level. However, we believe that volatility, while creating some challenges, will provide an attractive environment for long-term investors to back quality companies with attractive, sustainable income streams and long-term structural capital growth at reasonable valuations across the market cap spectrum. Across the UK equity income sector, we believe that there are likely to be compelling diversified, robust, and resilient income generating opportunities, that we are well positioned to uncover, appraise and deploy capital into. 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 over the long term, our fundamental focused investment style has the potential to outperform. The Fund will maintain its focus on building a high conviction portfolio of less cyclical, high-quality businesses with stable and growing earnings streams, good cash flows and dividends. We believe these businesses can deliver strong returns through the market cycle regardless of the performance of the wider economy.