Liontrust UK Smaller Companies Fund

April 2022 review

Fund managers: Matthew Tonge, Anthony Cross, Julian Fosh, Victoria Stevens and Alex Wedge

The Liontrust UK Smaller Companies Fund returned -2.2%* in April. The FTSE Small Cap (excluding investment trusts) Index comparator benchmark returned -0.9% and the average return of funds in the IA UK Smaller Companies sector, also a comparator benchmark, was -2.0%.

The narrative of rampant inflation and anticipation of the monetary response remained firmly entrenched during April. As US and UK consumer price inflation hit 8.5% and 7.0% respectively in March, consensus expectations for central bank rate hikes rose significantly. Much of this was due to the release of minutes from last month's US Federal Reserve rate-setting meeting which suggested some committee members would have preferred a 50bps rise to the 25bps implemented, were it not for uncertainty due to events in Ukraine.

News of fresh covid lockdown measures in parts of China also heightened existing concerns over global supply chains and input cost pressures for businesses.

The FTSE All-Share Index was able to register a monthly gain – led by the healthcare (+5.9%) and consumer staples (+4.4%) sectors - although it was notable that this strength derived from the large-caps: the FTSE 100 returned 0.8% while the FTSE 250 and FTSE Small Cap indices returned -1.8% and -1.2% respectively.

Amid an inflationary environment of relentless cost pressures, we believe the theme of pricing power will be critical. Our investment process specifically sets out to target those companies which possess enduring competitive advantage stemming from their intangible assets. As a consequence, many have strong pricing power which should stand the portfolio in good stead if inflation continues to spiral upwards.

From corporate newsflow and our meetings with companies, we believe that the majority of our holdings are proving resilient in their underlying trading so far this year, despite the well documented pressures of input cost inflation, supply chain shortages, logistical disruption and early signs of a squeeze on consumer spending and business sentiment.

Many have already proven themselves adept at leveraging their barriers to competition to pass on inflationary pressures to customers – something which will be critical to the relative success of companies over the coming months.

It is already apparent that this year's stock market turmoil and the de-rating experienced by many businesses will not go unnoticed by corporate and private equity buyers if it persists. During April, two holdings received potential takeover approaches: the third and fourth of 2022 for the Fund.

The Baring Private Equity Asia VIII Fund announced that it was considering an offer for **RWS Holdings** (+19%), although no formal approach had been made. The news pushed shares in RWS higher, but only really recouped the ground lost in March when its latest acquisition and strategy announcement underwhelmed investors. The news also overshadowed a trading update from RWS later in April in which it forecast adjusted profit before tax of at least £60m, slightly ahead of its prior expectations.

Similarly, private equity investor Cinven announced that it was considering an offer for **Ideagen** (+7.8%), but had not made a formal approach. Earlier this year, **Clipper Logistics** recommended a takeover offer from US-listed

GXO Logistics, while **CareTech** has announced the receipt of approaches from a founder-led consortium and a rival private equity bidder

The portfolio's biggest fall came at **Gear4Music** (-41%), after a year-end trading update revealed a 6% fall in sales during the period to 31 March and stated that earnings were also slightly lower than consensus expectations. Its disappointing full-year performance stems from weaker-than-expected consumer demand during February and March 2022. The retailer of musical instrument and music equipment now anticipates weak consumer confidence affecting trading through the first half of its new year and it has lowered its full-year growth targets as a result.

Fears of a post-lockdown drop from exceptional demand levels may also be responsible for the weakness in **Focusrite** (-24%), a specialist in hardware and software for the high-quality production of recorded and live sound. However, interims released in April commented that demand remains strong and on-track to allow Focusrite to meet full-year forecasts. While demand has dropped from the unprecedented levels seen at the peak of lockdown, Focusrite says it remains materially higher than pre-pandemic levels.

Learning Technologies (-19%) dropped as it delayed the publication of full-year results from 26 April to 3 May due to an additional balance sheet review required by auditors relating to the treatment of trade receivables. The company stated that the adjustment would have no impact on income statement, net assets or cash. In an accompanying trading update, Learning Technologies outlined 8% organic revenue growth during 2021 and stated that trading in the first quarter of 2022 has been strong and in-line with expectations.

Interim results from **AB Dynamics** (+34%) built on the reassuring trading update issued in March. The company is a designer, manufacturer and supplier of advanced testing and measurement solutions to the global automotive industry. It grew revenue by 38% in the six months to 28 February when compared with the covid-affected period a year earlier. Customer activity levels have remined positive throughout the period, with track testing demand driving growth in orders and revenues. AB Dynamics commented that operational output has not been affected by the challenging supply chain environment, while it has been able to mitigate cost inflation through price increases on its products. It is confident regarding the second half of its financial year, with a large order book providing visibility over much of the targeted revenue.

Defence and security technology mini-conglomerate **Cohort** (+20%) announced that one of its businesses had received two UK Ministry of Defence orders worth more than £9m. The orders involve hearing protection systems for use in armoured fighting vehicles and by close combat personnel.

Eckoh (+16%), the provider of secure payment products and customer contact solutions, moved higher after issuing a full-year trading update. Results for the year to 31 March are expected to be in line with consensus expectations after Syntec – its £31m acquisition in December 2021 – integrated well and made a good three-month contribution.

Positive contributors included:
AB Dynamics (+34%), Cohort (+20%), RWS Holdings (+19%), Netcall (+17%) and Eckoh (+16%).

Negative contributors included:
Gear4Music (-41%), Focusrite (-24%), Learning Technologies Group (-19%), Big Technologies (-19%) and Team17 Group (-19%).

Discrete years' performance (%), to previous quarter-end:**
Past performance does not predict future returns

	Mar-22	Mar-21	Mar-20	Mar-19	Mar-18
Liontrust UK Smaller Companies I Inc	2.6%	56.7%	-5.8%	1.9%	17.1%
FTSE Small Cap ex ITs	5.5%	74.9%	-24.4%	-3.1%	2.2%
IA UK Smaller Companies	-1.7%	65.7%	-17.9%	-2.6%	14.9%
Quartile	1	3	1	1	2

*Source: Financial Express, as at 30.04.22, total return (net of fees and income reinvested), bid-to-bid, institutional class.
**Source: Financial Express, as at 31.03.22, total return (net of fees and income reinvested), bid-to-bid, primary class.

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/glossary

Key Risks:

Past performance is not a guide to future performance. The value of an investment and the income generated from it can fall as well as rise and is not guaranteed. You may get back less than you originally invested.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

The portfolio is primarily invested in smaller companies and companies traded on the Alternative Investment Market. These stocks may be less liquid and the price swings greater than those in, for example, larger companies.

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