Liontrust UK Micro Cap Fund

July 2022 review

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

The Liontrust UK Micro Cap Fund returned 1.4%* in July. The FTSE Small Cap (excluding investment trusts) Index and the FTSE AIM All-Share Index comparator benchmarks returned 3.5% and 5.3% respectively. The average return of funds in the IA UK Smaller Companies sector, also a comparator benchmark, was 4.8%.

Following the worst monthly return of 2022 in June, the UK market bounced back with its best showing so far this year. With little change to the main macroeconomic narrative of monetary policy tightening in the face of inflationary pressures, it's hard to pinpoint a reason for the shift. Many of last month's key trends reversed: the FTSE 250 (+8.3%) significantly outperformed the FTSE 100 (+4.4%) and industrials (+11.2%) moved from one of the heaviest fallers to July's best-performing sector.

This year so far has seen a de-rating of stocks with high expected growth profiles and commensurate 'expensive' conventional share valuations. Much of this trend, which has impacted the Fund, has been driven by shifts in investor sentiment in response to macroeconomic conditions rather than stock-specific newsflow. We have previously commented that, while many of our holdings acknowledge strengthening economic headwinds (such as cost inflation and falling consumer confidence), most have so far proven resilient in their underlying trading. There were lots of company updates for us to digest in July, many of which were trading statements covering the first half of 2022. On the whole, these were supportive of our assessment that Fund holdings are showing good trading resilience amid a deteriorating economic environment.

A Q1 trading update from paper and advanced materials group **James Cropper** (+27%) showed a 36% year-on-year sales increase, with growth across all three divisions: Paper, Colourform and Technical Fibre Products (TFP). Although James Cropper says that management expectations for this financial year are currently unchanged, it notes that profits are currently tracking ahead of plan. While price rises have helped the paper division return to profitability after energy costs spiked last quarter, it is progress at its Technical Fibre Products unit that drove the strong performance.

The independent delivered wholesale business, **Kitwave** (+23%)**,** released interim results showing a 52% increase in revenues in the six months to 30 April. Demand was particularly strong at the end of the period as trading recovered from the pandemic more quickly than Kitwave had expected. There was a notably strong recovery in its vending, ambient and foodservice lines. The company also announced that trading since 30 April has been significantly ahead of its expectations**,** leading it to upgrade forecasts for the year to 31 October 2022.

Cerillion (+18%) announced the agreement of a 10-year contract, worth around £15m, with a new telecoms customer. Cerillion provides software-as-a-service solutions for billing, charging and customer relationship management.

Although **CML Microsystems** (+14%) had already flagged in April that last year's trading had been slightly ahead of market expectations, it still made ground on the release of full-year results. The developer of mixed-signal, RF and microwave semiconductors for global communications markets recorded revenue growth of 29% to £17m as its end markets recovered, particularly in the voice-centric markets. Better product mix and tight cost control helped push profit before tax to £1.7m after a flat result last year. The company also commented that the new financial year has started well, with a strong order book that stretches beyond 12 months.

Fonix Mobile (+13%) disclosed robust trends within a full-year trading update. It grew adjusted EBITDA (earnings, before interest, tax, depreciation and amortisation) by 16% to £10.3m in the year to 30 June after active customers rose by 11% to 123 over the year. The mobile payments and messaging provider also commented that it ended the year with a strong exit run-rate and a growing pipeline of client prospects, giving it confidence regarding the new financial year.

The Fund's July fallers were headed by **CMO Group** (-65%), whose weakness was triggered by a profit warning. But the other detractors mostly commented on robust current trading but made cautious outlook statements.

Although total sales grew 10% in the first half of 2022, including 2% like-for-like expansion, **CMO Group** warned that higher transport and product costs have begun to soften its margins since Easter. The online retailer of building materials expects these headwinds to persist into the second half of this year and first half of 2023. As a result, it has reduced this year's revenue growth forecast to 13% and expects adjusted EBITDA to be flat on last year's level.

Revenue in the first half of 2022 was in line with **Attraqt Group's** (-18%) expectations at £12.1m, with sales momentum seeing its contract win rate improve. However, its trading update also included cautious outlook comments. The ecommerce online search specialist expects the deteriorating outlook for consumer-facing businesses to delay some customer decisions and lead times on enterprise sales to lengthen.

An AGM update from **Vianet Group** (-15%) stated that revenue momentum at the back end of last year has continued into its new financial year (starting on 1 April). Vianet provides data and analysis to pubs and vending machine operators via its connected 'internet-of-things' (IoT) platform. Its Smart Zones stock and waste management service for drinks retailers has seen very good growth, and is heading towards pre-pandemic levels. However, it is experiencing higher hardware costs due to the global semi-conductor supply shortages – an impact it has decided to absorb rather than pass on it as it pursues sales growth.

Another AGM update saw **Surgical Innovations Group** (-14%) comment that strength in the final quarter of 2021 has carried over to the first half of 2022, with revenues 22% ahead of last year's comparable. The specialist in medical technology for minimally invasive surgery thinks this momentum is continuing into the second half of the year and has maintained its full-year guidance. These positive messages were offset by warnings around labour market inflation, a shortage of skilled labour and supply chain challenges. These have extended sales order lead times and constrained manufacturing productivity, leading to an increase in the company's back orders.

Finally, **Frenkel Topping Group** (-15%) shares slipped as it conducted a placing to raise £10m to fund acquisitions. The company has already identified three potential targets and is on the lookout for more as it seeks to consolidate the fragmented pre-settlement professional services market for personal injury and clinical negligence. The placing price of 70p was a 10% discount to the prevailing share price, and shares in the secondary market moved a little lower to reflect the dilution. Frenkel Topping previously conducted a placing in July 2020 to raise £13m which it successfully used to finance its acquisitive growth strategy.

The position in **Medica** was sold as a consequence of its senior management equity ownership falling below the 3% threshold level required of all smaller companies held under the Economic Advantage process.

Positive contributors included:
James Cropper (+27%), Kitwave Group (+23%), Cerillion (+18%), CML Microsystems (+14%) and Fonix Mobile (+13%).

Negative contributors included:
CMO Group (-65%), Attraqt Group (-18%), Vianet Group (-15%), Frenkel Topping Group (-15%) and Surgical Innovations Group (-14%).

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

	Jun-22	Jun-21	Jun-20	Jun-19	Jun-18
Liontrust UK Micro Cap I Acc	-15.9%	59.5%	4.6%	3.1%	21.4%
FTSE Small Cap ex ITs	-14.6%	65.2%	-12.3%	-8.6%	6.4%
FTSE AIM All Share	-29.0%	42.5%	-2.8%	-13.9%	13.5%
IA UK Smaller Companies	-22.1%	53.1%	-6.5%	-6.2%	17.2%
Quartile	1	2	1	1	1

*Source: Financial Express, as at 31.07.22, total return (net of fees and income reinvested), bid-to-bid, institutional class.
**Source: Financial Express, as at 30.06.22, total return (net of fees and income reinvested), bid-to-bid, institutional 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.