GLOBAL EQUITY

Liontrust Global Smaller Companies Fund

Q3 2022 review

Fund manager: Robin Geffen & Deputy Will Geffen

The Liontrust Global Smaller Companies Fund returned 3.9% over the quarter, versus the MSCI ACWI Small Cap Index and IA Global sector respective returns of 3.1% and 1.8% (both comparator benchmarks)*.

We continue to be positive on the outlook for high quality smaller companies that we believe are capable of exponential growth. We are especially positive as the smaller companies area of the market continues to give considerable scope for further outperformance as the world continues to recover from the Covid-19 pandemic. Smaller companies, particularly in the US, enjoy a lower valuation rating than their large and mega cap peers, which we believe can be translated into continued strong returns. We believe these companies can future-proof a portfolio by using the five drivers of Science, Intellectual Property, Deep Technology, Positive Change and Entrepreneurial Vision. The fast-growing business we invest in are typically capital light and built upon these five key drivers. This leads us to avoid sectors, sub-sectors, and stocks that are capital intensive, as larger and existing companies have a huge advantage. We believe these sectors include traditional real estate, utilities, mining and oil and gas exploration, integrated oil and gas companies, tobacco companies and arms manufacturers. In addition, within the finance sector, we prefer to avoid capital intensive stocks such banks and traditional insurance businesses.

After a rally in July, both equity and bond markets performed poorly in the second half of the quarter, as several interrelated factors look to drag the global economy into a recession. These intertwined headwinds include high inflation from years of loose monetary policy and meeting the supply shock from Covid along with resurgent post-Covid demand. The war in the Ukraine adds geopolitical uncertainty as well as scarcity to energy and key raw materials from trade sanctions with Russia. Harsh lockdowns in China have stalled economic growth in the world's second largest economy and a key link in supply chains. Finally, central bank tightening to combat high inflation is leading the economy away from over a decade of low (and steadily decreasing) interest rates.

In terms of stock attribution, **Workiva**, a maker of software for regulatory, financial and environmental, social and governance reporting, was among the notable contributors over the period, after the company drew takeover interest from private equity firms – with Thoma Bravo and TPG among firms that have reportedly held discussions.

CyberArk was another notable outperformer over the quarter, with cybersecurity remaining a more "defensive" corner of the software market. Our market research shows that despite economic uncertainty, CIOs are not planning on reducing the cybersecurity software budgets – opting for nearly cutting every other expense first. The tough security climate, combined with immense career risk for operators and executives means that cybersecurity remains a favoured theme for the foreseeable future.

On the other side of the ledger, rising interest rates continue to negatively impact the ratings of higher growth stocks in our portfolio, but the companies themselves remain more or less individually unaffected. **Rapid7** is one such business operating in cybersecurity, which is anticipating solid 20%+ growth for the foreseeable future, however, has been harshly derated in the recent selloff in software.

Verint Systems had a decent run this year until it produced disappointing Q2 earnings in September where revenue missed consensus, but, critically, cloud revenue (a large driver of stock sentiment due to higher cloud SaaS ratings) disappointed with growth coming in far short of the previous quarter. Combined with harsh FX headwinds and the CFO stepping down, the stock has fallen substantially. We do however still believe that the outlook is still favourable; we expect steady growth combined with steady durable margins, allowing the stock to rerate as cloud becomes a larger percentage of sales.

Yeti has seen a substantial derating over the last year as the Covid-induced jump in enthusiasm for outdoor leisure activities starts to subside with tough year-on-year comparators. The two key long-term drivers remain in place: interest in outdoor leisure continues to grow; and the Yeti brand remains strong, capturing a large amount of web and foot traffic and catering to the full spectrum of outdoor enthusiasts.

IAS, **Smartsheet**, and **Pegasystems** were all unfortunately sold to due to triggering our stop loss rules. We began exiting the positions as they deteriorated and are currently reassessing their investment case in light of their substantial underperformance of the rest of the portfolio.

In addition, **SailPoint** was exited after and attractive takeout deal from PE investors, Thoma Bravo, was finalised. The portfolio has seen several companies bought by PE investors as they fall to very attractive long-term valuations. Such examples include Datto which was acquired in the second quarter, and earlier in the year we saw Microsoft buy Nuance Communications, showing that the highest quality growth companies also remain attractive takeover targets for even the very largest mega caps if they have high quality intellectual property. This highlights the extraordinary value available in these high quality smaller companies that we aim to invest in.

Using the capital from the SailPoint deal and other exits, we entered a range of new positions ranging from **Mandarin Oriental** – which operate a leading brand in high-end hotels set to benefit from the post covid resurgence in corporate and luxury travel – to security software vendor **Clear Secure**, online dating platform **Bumble**, marketing specialist **Double Verify**, silicon carbide chip producer **Wolfspeed**, and **Masimo**, a previous holding in the Fund which owns a lucrative niche in medical equipment, selling blood oximeters. These companies offered compelling entry points given the recent market drawdown and we believe they should offer investors strong returns for the foreseeable future.

While the markets and economic outlook may look bleak on the surface, it is hard not to be excited by the current landscape for investors. The global small cap universe now presents a large number of fantastic companies available for purchase at a cash yield not seen for many years. This, combined with much lower coverage by broker and investors presents a great opportunity for long-term, alpha-seeking active investors.

Now, as ever, it is important to actively seek high performing companies. By focussing on a companies with key financial metrics that support a strong investment narrative and provide an attractive discounted cash flow valuation, we aim to help provide long term outperformance through careful and attentive active management.

We continue to believe that our emphasis on the drivers of Science, Intellectual Property, Deep Technology, Positive Social Change and Entrepreneurial Vision will, guide the Fund towards those companies that will change the world as we adapt in future.

Discrete years' performance (%), to previous quarter-end:**

	Sep-22	Sep-21	Sep-20	Sep-19	Sep-18
Liontrust Global Smaller Companies C Acc GBP	-24.9%	25.0%	31.7%	-2.9%	32.8%
MSCI ACWI Small Cap	-9.2%	34.8%	-1.6%	0.1%	11.8%
IA Global	-8.9%	23.2%	7.2%	6.0%	11.6%

Quartile	4	2	1	4	1

***Source: FE Analytics as at 30.09.22**

****Source: FE Analytics as at 30.09.22. Quartiles generated on 07.10.22**

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

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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 invested in smaller companies - these stocks may be less liquid and the price swings greater than those in, for example, larger companies. Investment in the Fund involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. The Fund may invest in emerging markets/soft currencies or in financial derivative instruments, both of which may have the effect of increasing volatility. The Fund holds a concentrated portfolio of stocks, if the price of one of these stocks should move significantly, this may have a notable effect on the value of the portfolio.