LIONTRUST

GLOBAL EQUITY

Liontrust Global Smaller Companies Fund

Q4 2022 review

Fund Manager: Robin Geffen & Deputy Will Geffen

The Liontrust Global Smaller Companies Fund returned -2.6% over the quarter, versus the MSCI ACWI Small Cap Index and IA Global sector respective returns of 2.5% and 2.2% (both comparator benchmarks)*. Part of the Fund's underperformance relative to the sector can be attributed to a weaker sterling recovering 8% versus the dollar over the quarter.

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.

We continue to believe that active and disciplined stock selection can deliver sustained outperformance, shown by the long-term performance of the Fund, which has returned 43.0% over five years versus the MSCI ACWI Small Cap return of 31.8% and 38.7% return from the IA Global sector. Since the change of the Fund's strategy on 30th June 2016, the Fund has returned 102.4% versus the MSCI ACWI Small Cap's 76.1% and IA Global's 82.7%, placing the Fund in the top quartile for the period.

Equity markets stabilised and showed some signs of recovery this quarter, with hopes of an earlier than expected fed pivot, or "soft landing" easing the market as early signs show US inflation beginning to ease. Many companies, however, are still bracing for a slowdown and a raft of downwards earnings revisions across the board does seem likely in the early half of 2023.

Among the top performers for the fourth quarter were Box Inc., Evoqua Water Technologies and Games Workshop. These positions all experienced tough Q3 drawdowns but rebounded nicely in Q4. Box has experienced a strong rebound from September by continuing to drive margin gains as well as growth in the Japanese market that has continued to impress markets. Similarly, Evoqua's Q3 earnings showed continued revenue, profit and cashflow growth as it continues to deliver on its impressive environmental mission of essential waste water treatment.

Games Workshop – a UK based company, also rebounded from a September low that saw it drop 40% from the beginning of 2022. It has since recovered, not least as UK markets and outlook have rebounded after significant period of political and fiscal uncertainty. While the UK economic environment remains challenging, Games Workshops international reach and pivot towards lower cost digital IP assets with broader appeal (video games as opposed to physical models) should see it do well despite.

Cybersecurity stocks held up in the face of a strong drawdown in tech equities – largely due to the resilience of both corporate IT spend and cybersecurity's share within that. Unfortunately, the sector had had a poor Q3 earnings season, pointing to the economic downturn putting pressure on smaller companies to delay further purchases and "right size" deals which had been previously allowed to be wider in scope and spend. These stocks (Rapid7 and CyberArk) are owned and valued as a high growth companies and so it is of no surprise, therefore, that fears of substantial slowdown in growth will have a large impact on valuation. We remain confident, however that the core products and businesses remain strong and stand to benefit from the ongoing steady growth trend in cybersecurity spend.

In terms of portfolio activity, we exited positions in Zuora and Upwork over the fourth quarter. Both Zuora and Upwork were positions that had tripped our stop loss alerts earlier this year causing us to reassess their prospects. Both companies are highly leveraged to the technology ecosystem – Zuora through managing subscription monetisation, and Upwork through helping with talent acquisition via its freelancer network. Both of these companies are therefore highly indexed to the health of the Silicon Valley and broader start-up ecosystem for additional growth. With the current "Patagonia vest recession" impacting the tech ecosystem and venture financing drying up, we expect these companies may struggle to recoup losses in the near future. We will continue to monitor these companies for future opportunities when the environment shifts.

With regard to additions, we initiated positions in Topicus.com and RXO (via spinoff from XPO).

Topicus.com is a spinout of our portfolio company Constellation Software (who still retain a healthy % ownership). Topicus, like Constellation, is a serial acquirer of VMS companies, benefitting from the fantastic economics of these businesses and cycling their cash into further high ROI M&A that benefits from an incredible track record of capital discipline and value creation.

RXO was spun from portfolio company XPO logistics and represents its 3rd party brokerage business. XPO is a fantastic logistics and transportation business, and this spinoff represents an opportunity to directly invest in one of the best businesses in the XPO collection – the high margin, asset light tech platform that connects shippers and independent carriers in a way that maximises cost and fuel efficiency for both parties.

While 2022 saw a tough year for equities – especially for stocks of smaller higher growth companies, it has set the playing field for an interesting 2023.

Markets and economic may look bleak on the surface, it is hard not to be excited by the current state of affairs for investors in the smaller innovative companies. The smaller cap universe, already a stock pickers paradise, now presents a large number of fantastic companies available for purchase at a price not seen for a long time – a great setup for long-term outperformance.

While markets do move somewhat at the mercy of large forces like interest rates, inflation and economic health (at least in the short term) – the rewards are looking ever more asymmetrically favourable for investors in innovative smaller companies. The downside scenarios (aggressive rate hikes, high inflation, economic downturn) are fairly priced in with strong returns likely in the eventuality of a soft landing, tamed inflation and economic rebound.

Taking all of this into account, we continue to believe very strongly that the long-term prospects of the high-quality companies we own, and thus the performance of the Fund, will continue to be driven by the 5 key drivers of Science, Intellectual Property, New Deep Technology, Positive Change and Entrepreneurial Vision.

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

	Dec-22	Dec-21	Dec-20	Dec-19	Dec-18
Liontrust Global Smaller Companies C Acc GBP	-27.1%	8.0%	48.0%	20.1%	2.2%
MSCI ACWI Small Cap	-8.4%	17.2%	12.7%	19.8%	-9.1%
IA Global	-11.1%	17.7%	15.3%	21.9%	-5.7%
Quartile	4	4	1	3	1

***Source: FE Analytics as at 31.12.22**
****Source: FE Analytics as at 31.12.22. Quartiles generated on 06.01.23**

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

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.

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