

Liontrust Special Situations Fund

August 2023 review

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The Liontrust Special Situations Fund returned -1.6%* in August. The FTSE All-Share Index comparator benchmark returned -2.5% and the average return in the IA UK All Companies sector, also a comparator benchmark, was -2.2%.

The Bank of England implemented its 14th successive hike in this tightening cycle, taking interest rates to 5.25%. Wage and inflation data released later in the month confirmed the view that one or two more increases are likely to be needed before rates top out.

During August, investors were also paying close attention to trends in China, where interest rates are moving in the other direction. Having gradually disappointed this year against expectations of a post-Covid lockdown bounce in activity, China's economic woes weighed on investor sentiment during the month. China's central bank responded by lowering its one-year loan rate – the 'medium-term lending facility' – by 15 basis points, in a move that surprised markets and economists alike..

The UK market experienced broad-based declines with some pockets of deeper weakness in areas with greater exposure to Chinese demand – such as basic materials (-5.9%) and consumer discretionary (-3.3%).

As briefly covered in last month's review, **Domino's Pizza Group** (+15%) released a strong set of interim results on the first day of August. Like-for-like sales growth of 7.9% year-on-year was ahead of expectations. A programme of store openings has been accelerated, with 11 franchise partners opening 29 stores, helping boost total sales growth to 20%. With robust trading carrying over to the first weeks of July, Domino's issued full-year earnings guidance which was about 5% ahead of analyst consensus forecasts.

Last month, Domino's removed some succession uncertainty by announcing Andrew Rennie as its new CEO, having operated with an interim CEO since late last year. Rennie's appointment was received with enthusiasm by investors, given his high calibre and significant previous experience across the Domino's global empire: he was previously a successful multi-unit franchisee for a decade, and then spent over two decades at the Sydney-listed Domino's Pizza Enterprises in multiple roles, overseeing a very strong period of growth at the business.

Industrial thread manufacturer **Coats Group** (+10%) had already warned in a May trading update of a fall in sales this year as customers destocked in reflection of subdued consumer demand and high inventory levels. Interim results showed an organic drop in sales of 19% in the first half of 2023. Including sale contributions from its recent footwear acquisitions – Texon and Rhonoflex – brings the sales drop to a more moderate 11%. While volumes may be under pressure, investors took heart from better-than-expected operating profit margins of 15%, up 30 basis points on the same period last year. Outlook comments were also encouraging, with Coats expecting volumes to gradually recover from current levels.

Paypoint (+11%) shares have enjoyed good momentum since a June trading update which outlined strong financial performance in the year to 31 March, including an upgrade to profits guidance. Previously, shares in the convenience store payments and e-commerce specialist had de-rated following the announcement late last year of a deal to buy gift card group Appreciate. The recovery was further aided by a trading update on 31 July which showed strong revenue growth of 20% in the three months to 30 June.

Having seen its shares jump in February due to bid interest from Apollo, only to tumble in May as the private equity group walked away, **John Wood Group** (+8.1%) was able to regain some impetus on the back of contract

momentum and robust interims. Firstly, the consulting and engineering group announced the award of a multi-year extension to its relationship with Shell. Although no financial details were disclosed, the deal covers Shell's global projects for a three-year period, with options for two one-year extensions. It then announced revenue growth of 16% to £3.0bn in the first half of 2023, with adjusted operating profit rising 9% to £89m. Although revenue growth is expected to slow in the second half, earnings are now on track to be ahead of the company's prior expectations.

While excitement over artificial intelligence (AI) has boosted stockmarkets this year, particularly in the US, these gains have been very concentrated in a few tech giants. Investors have also attempted to identify the 'losers' from AI's accelerated uptake and mark down their share prices accordingly. As a provider of a range of outsourced support services to the video game industry, **Keywords Studios** (-14%) is one of those that has been singled out.

Despite a solid trading statement released at the beginning of the month, showing organic revenue growth of 10% in the first half of the financial year and an adjusted operating margin of 15%, in line with guidance, Keywords' shares slumped further in August and have now dropped around 40% this year. With the shares trading on around half their long run average valuation, we believe the pronounced fall has been overdone. As for many other companies perceived to be 'at risk' of existential threat from AI advances, the reality for Keywords is likely to be more nuanced than these sometimes violent shifts in sentiment might suggest. AI may yet prove to be a significant opportunity as well as a threat, if the business can harness its market leadership position and deep customer relationships to employ AI to drive efficiencies for themselves and their customers.

Positive contributors included:

Domino's Pizza Group (+15%), Paypoint (+11%), Coats Group (+9.6%), John Wood Group (+8.1%) and Sage Group (+3.7%).

Negative contributors included:

Keywords Studios (-13.5%), Hargreaves Lansdown (-11%), YouGov (-10%), IMI (-7.3%) and Renishaw (-6.7%).

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

Past performance does not predict future returns

	Jun-23	Jun-22	Jun-21	Jun-20	Jun-19
Liontrust Special Situations I Inc	6.8%	-11.0%	24.6%	-7.7%	6.5%
FTSE All Share	7.9%	1.6%	21.5%	-13.0%	0.6%
IA UK All Companies	6.2%	-8.5%	27.7%	-11.0%	-2.2%
Quartile	3	3	3	2	1

*Source: Financial Express, as at 31.08.23, total return (net of fees and income reinvested), bid-to-bid, institutional class.

**Source: Financial Express, as at 30.06.23, 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.

A proportion of the portfolio is 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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