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Economic Advantage

February 2024 review

Liontrust UK Smaller Companies Fund

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The Liontrust UK Smaller Companies Fund returned -2.0%* in February. The FTSE Small Cap (excluding investment trusts) Index comparator benchmark returned -1.4% and the average return of funds in the IA UK Smaller Companies sector, also a comparator benchmark, was -1.5%.

The UK market's lack of impetus in February coincided with the official confirmation that the UK entered a technical recession at the end of 2023 – a fate that is yet to befall the US despite being expected to arrive for most of the last year. However, investors and therefore share prices are famously forward looking, and none of this year's lack of stock market direction is attributable to last year's economic contraction, which is both minimal in scale (-0.3% in Q3 and -0.1% in Q4) and very much in the rear-view mirror.

Instead, expectations regarding the future direction of interest rates once again seem largely responsible, with the late-2023 confidence in imminent rate cuts starting to ebb away under pressure from stubbornly high inflation readings.

It was a quieter month for portfolio news flow than January, but there were still a number of company updates for us to stay abreast of.

Intellectual property support services provider **RWS Holdings** (-13%) suffered in 2023 due to macro-related delays to decision-making among some customers – contributing to cuts to financial forecasts – and wider market concerns about the impact of generative AI models. Its shares slid further in February despite a short AGM statement which was reassuring in tone. While acknowledging that macroeconomic challenges remain, RWS has maintained its 2024 outlook, with client retention remaining high and the company seeing some early contract wins at enterprise-level clients for its recently developed Evolve linguistic AI solution.

Another detractor was **LSL Property Services** (-11%), after disclosing that subdued activity levels across the valuation market continue to impact its Surveying division. However, there were signs of improvement toward the end of 2023. LSL's Estate Agency unit – recently converted to a wholly franchise model – performed ahead of expectations in 2023, while its Financial Services Network was also slightly more profitable than forecast.

Overall, 2023 revenue fell 10% like-for-like. The company expects 2024 to see a material increase in profits as surveying activity picks up.

In more upbeat news, Animalcare (+25%) rallied as it announced the disposal of a non-core, majority shareholding in UK-based pet microchipping company Identicare for a cash consideration of £24.9m. The price obtained for the business positively surprised investors, and now allows Animalcare to focus on growth on its animal pharmaceuticals business – in keeping with the strategic decision in 2021 to separate the two units into different operating divisions.

We have spoken in previous reviews about unusually low valuations triggering an acceleration in merger and acquisition activity across the market. The Fund exited its position in Smart Metering Systems following the board's recommendation of a cash takeover offer of 955p from private equity group KKR at a 40% premium to the previous share price close. The deal is expected to complete imminently and shares in the company traded close to the offer terms, allowing us to exit the position and seek to redeploy the capital.

Positive contributors included:

Animalcare (+25%), Nexteq (+17%), Judges Scientific (+16%), Fevertree Drinks (+14%) and Bioventix (+12%).

Negative contributors included:

Focusrite (-18%), RWS Holdings (-13%), Impax Asset Management (-13%), LSL Property Services (-11%) and Globaldata (-11%).

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

	Dec-23	Dec-22	Dec-21	Dec-20	Dec-19
Liontrust UK Smaller Companies I Inc	-0.8%	-23.0%	24.7%	15.2%	31.0%
FTSE Small Cap ex ITs	10.4%	-17.3%	31.3%	1.7%	17.7%
IA UK Smaller Companies	0.5%	-25.2%	22.9%	6.5%	25.3%
Quartile	3	2	2	1	2

*Source: Financial Express, as at 29.02.24, total return (net of fees and income reinvested), bid-to-bid, institutional class. **Source: Financial Express, as at 31.12.23, 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/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance does not predict future returns. You may get back less than you originally invested. We recommend this fund is held long term (minimum period of 5 years). We recommend that you hold this fund as part of a diversified portfolio of investments.

The Fund may invest in companies listed on the Alternative Investment Market (AIM) which is primarily for emerging or smaller companies. The rules are less demanding than those of the official List of the London Stock Exchange and therefore companies listed on AIM may carry a greater risk than a company with a full listing.

As the Fund is primarily exposed to smaller companies there may be liquidity constraints from time to time, i.e. in certain circumstances, the fund may not be able to sell a position for full value or at all in the short term. This may affect performance and could cause the fund to defer or suspend redemptions of its shares. In addition the spread between the price you buy and sell units will reflect the less liquid nature of the underlying holdings.

Outside of normal conditions, the Fund may hold higher levels of cash which may be deposited with several credit counterparties (e.g. international banks). A credit risk arises should one or more of these counterparties be unable to return the deposited cash.

Counterparty Risk: any derivative contract, including FX hedging, may be at risk if the counterparty fails.

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.

Disclaimer